S. Hrg. 101-259, Pt. XIII

PREPARATION FOR THE 1990 FARM BILL

HEARINGS

BEFORE THE

SUBCOMMITTEE ON AGRICULTURAL PRODUCTION
AND STABILIZATION OF PRICES

OF THE

COMMITTEE ON AGRICULTURE,
NUTRITION, AND FORESTRY
UNITED STATES SENATE

ONE HUNDRED FIRST CONGRESS

SECOND SESSION

ON

CROP INSURANCE; WHEAT; DEFICIENCY PAYMENT PROBLEMS
ASSOCIATED WITH BARLEY; AND COST OF PRODUCTION

MARCH 6 AND 8, 1990
APRIL 19 AND 23, 1990

PART XIII

Printed for the use of the
Committee on Agriculture, Nutrition, and Forestry

U.S. GOVERNMENT PRINTING OFFICE
42-184 ⇆ WASHINGTON : 1991

S161-24

For sale by the Superintendent of Documents, Congressional Sales Office
U.S. Government Printing Office, Washington, DC 20402

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CONTENTS

Page

Hearings held on:
  March 6, 1990 1
  March 8, 1990 195
  April 19, 1990 377
  April 23, 1990 445

TUESDAY, MARCH 6, 1990

PREPARATION FOR THE 1990 FARM BILL

Crop Insurance

Pryor, Hon. David H., a U.S. Senator from Arkansas 1
Conrad, Hon. Kent, a U.S. Senator from North Dakota 23
  Prepared statement 3
Baucus, Hon. Max, a U.S. Senator from Montana 2
  Prepared statement 3
Bond, Hon. Christopher S. "Kit", a U.S. Senator from Missouri 33

CHRONOLOGICAL LIST OF WITNESSES

Mikulski, Hon. Barbara A., a U.S. Senator from Maryland 5
  Prepared statement 8
  Report on Federal Crop Insurance to Governor William Donald Schaefer .. 10
Kislak, Jonathan I., Deputy Under Secretary, U.S. Department of Agriculture, Washington, DC 24
  Prepared statement 37
  Attachment A—Federal Crop Insurance Corporation Comparative Program Highlights for Crop Years 1987, 1988 and 1989 41
  Rutledge, Perry, president, Farmers Mutual Hail Insurance Company of Iowa, letter of, dated February 9, 1990, with enclosed article, "A New Kind of Crop Insurance," to Hon. Clayton Yeutter 42
Harman, John W., Director, Food and Agriculture Issues, Resources, Community, and Economic Development Division, U.S. General Accounting Office, Washington DC; accompanied by Cliff Fowler, Assistant Director; and Jeffrey W. Itell, Evaluator-In-Charge 45
  Prepared statement 56
  Chart 1—Government Costs for Agriculture Disaster Assistance Programs (FY 1980–88) 70
  Chart 2—Government Costs for Direct Payment, Emergency Loan, and Crop Insurance Programs (FY 1980–88) 71
  Appendix I—Chart Showing How Well Different Forms of Disaster Assistance Meet the Criteria 72
Davis, Ray, Cochairman, Commission for the Improvement of the Federal Crop Insurance Program, wheat farmer, Potter, NE 74
Classen, Bill, Cochairman, Commission for the Improvement of the Federal Crop Insurance Program, president, Rain and Hail Insurance Service, Inc., Des Moines, IA 77
  Prepared joint statement of Ray Davis and Bill Classen 87

Page
Classen, Bill, Cochairman, Commission for the Improvement of the Federal Crop Insurance Program, president, Rain and Hail Insurance Service, Inc., Des Moines, IA—Continued
  Attachments:
    A—Summary of Recommendations, from Commission's Interim Report, April 1989 102
    B—Executive Summary of Recommendations, from Commission's Principal Report, July 1989 105
    C—Summary of Proposal for an Alternative Program 108
    D—Subsequent Recommendations 111
Rahjes, Doyle, American Farm Bureau Federation, president, Kansas Farm Bureau Federation, Agra, KS 113
Jones, Corky, on behalf of the American Agriculture Movement 115
Senter, David, national director, American Agriculture Movement, prepared statement 118
Giessel, Tom, National Farmers Union, vice president, Kansas Farmers Union, Washington, DC 123
  Prepared statement 126
  Special Order of Business 130
Claybaker, Max J., wheat farmer, insurance agent, Blackwell, OK 131
  Prepared statement 134
Gibson, Richard C., chairman, American Association of Crop Insurers, Council Bluffs, IA; accompanied by Paul Friskopp, insurance agent, Shelton, NE, and Ruth Gerdes, insurance agent, Auburn, NE 138
  Prepared statement 141
  1989 U.S. MPCI Participation—All Crops, chart 144
  Winter Wheat Participation Growth—Major States, chart 145
  MPCI Made Simple—Dollar Coverage Plan 146
Bracey, Bill, National Association of Professional Insurance Agents, Bracey Insurance Agency, Blytheville, AR 148
  Prepared statement 149
Beal, Ralph D., president, Master Marketers' Association of America, Honey Grove, TX, prepared statement 165
  Exhibits A-E 177
  Association membership 186
Vohs, George F., president, LongView Insurance Companies, Greeley, CO, prepared statement 187
Federal Register, vol. 55, No. 40, Wednesday, February 28, 1990, Interim rule 192

THURSDAY, MARCH 8, 1990

PREPARATION FOR THE 1990 FARM BILL

WHEAT

Boren, Hon. David L., a U.S. Senator from Oklahoma 195
Conrad, Hon. Kent, a U.S. Senator from North Dakota 200
Daschle, Hon. Thomas A., a U.S. Senator from South Dakota 201
Baucus, Hon. Max, a U.S. Senator from Montana 197
Dole, Hon. Robert, a U.S. Senator from Kansas, prepared statement 202
Cochran, Hon. Thad, a U.S. Senator from Mississippi 202
Boschwitz, Hon. Rudy, a U.S. Senator from Minnesota 201
Bond, Hon. Christopher S. "Kit", a U.S. Senator from Missouri, prepared statement 203
Gorton, Hon. Slade, a U.S. Senator from Washington 199

CHRONOLOGICAL LIST OF WITNESSES

McClure, Hon. James A., a U.S. Senator from Idaho, prepared statement 204
Gardner, Bruce L., Assistant Secretary for Economics, U.S. Department of Agriculture, Washington, DC 205
  Prepared statement 223
  Charts and tables 239
Tierney, William I., Jr., department of agricultural economics, Kansas State University, Manhattan, KS 246
  Prepared statement 252
  Detailed analysis of the wheat situation, prepared testimony of 265

Page
Wyckoff, Reggie, past president, National Association of Wheat Growers, Genoa, CO 288
  Prepared statement 291
Schupbach, Louis, president, Oklahoma Wheat Growers Association, Alva, OK 294
  Prepared statement 297
  Footnotes 306
Dilse, Frank, vice president, North Dakota Grain Growers Association, Scranton, ND 308
  Prepared statement 310
Marten, Randy, vice president, materials acquisition and transportation, Campbell Taggart Inc., Dallas, TX; representing American Bakers Association, Washington, DC 313
  Prepared statement 315
  Attached February 22, 1990, prepared statement 320
Goulding, Stephen H., president, Oak State Products, Inc., Wenona, IL; testifying on behalf of the Biscuit and Cracker Manufacturers' Association (B&CMA), Washington, DC 325
  Prepared statement 327
  1990 Farm Bill Position Paper 332
Lyons, David, member, board of directors, North American Export Grain Association (NAEGA), Washington, DC 339
  Prepared statement 342
  The Export Enhancement Program (EEP): A Proposal for Change 349
Fischer, Duane A., president and chief executive officer, Scoular Grain Co., Omaha, NE; testifying on behalf of National Grain and Feed Association, Washington, DC 353
  Prepared statement 356

THURSDAY, APRIL 19, 1990

PREPARATION FOR THE 1990 FARM BILL

Deficiency Payment Problems Associated With Barley Production

Baucus, Hon. Max, a U.S. Senator from Montana 377

CHRONOLOGICAL LIST OF WITNESSES

McClure, Hon. James A., a U.S. Senator from Idaho, prepared statement 378
Bjerke, Keith, Administrator, Agricultural Stabilization and Conservation Service (ASCS), U.S. Department of Agriculture, Washington, DC 379
Paul, George V., executive director, Montana Farmers Union, Great Falls, MT 385
  Prepared statement 390
Lacey, Gerald A., president, Minnesota Barley Growers Association, Campbell, MN 395
  Prepared statement 398
Jones, Marsha, national grains chairperson, Women Involved in Farm Economics (WIFE), Grover, CO 404
  Prepared statement 408
Naught, Stephen, vice president, National Barley Growers Association, Bickleton, WA 412
  Prepared statement 416
  Evaluation of Barley Target Price Utilizing Nutritional Analysis and Market Data 420
  Table 1.—Barley Disappearance, Marketing Years 1984/85 Through 1988/89 422
  Table 2.—Average Barley Price Received by Farmers, Marketing Years 1984/85 Through 1988/89 423
  Table 3.—Barley Fed by Livestock Class 424
  Table 4.—Selected Feed Composition of Barley, Corn, and Soybean Meal, Dry Matter on an As-Is Basis 425
  Table 5.—Soybean Meal, 44 Percent Protein: Prices Paid, U.S. Basis 426
  Figure 1.—Development of Feed Value of Barley in Relation to Corn 427
  Table 6.—Barley Feed and Malting Price Comparison to 1990 Corn Target Price 428

Page

- McGreevy, Tim D., administrator, Idaho Barley Commission, Boise, ID 429
  - Prepared statement 433
  - Chart No. 1.—History of Target Prices (1980–1990) 434
  - Chart No. 2.—Target Prices as a Percentage of Economic Cost of Production 436

MONDAY, APRIL 23, 1990

PREPARATION FOR THE 1990 FARM BILL

COST OF PRODUCTION

- Pryor, Hon. David H., a U.S. Senator from Arkansas 445
  - U.S. Consumers Spend Less on Food Than Consumers in Any Other Country, table 537
  - Charts:
    - Food Costs Worldwide 1989 538
    - U.S. Rice Production Costs 539
    - U.S. Soybean Production Costs 540
    - U.S. Cotton Production Costs 541
    - U.S. Peanut Production Costs 542
    - U.S. Corn Production Costs 543
    - U.S. Sugar-Beet Production Costs 544
    - U.S. Oats Production Costs 545
    - U.S. Cow-Calf Production Costs 546
    - U.S. Wheat Production Costs 547
    - Cost of Farm Equipment (autos & trucks) 548
- Baucus, Hon. Max, a U.S. Senator from Montana 451

CHRONOLOGICAL LIST OF WITNESSES

- Tull, John, rice farmer, Lonoke, AR 447
- Griggs, Billy, peanut farmer, Unadilla, GA 453
  - Prepared statement 455
  - Chart 1—Georgia Average Cost Per Acre (Peanuts) 457
  - Chart 2—Georgia Yield Per Acre (Peanuts) 458
  - Chart 3—Georgia Average Cost Per Pound (Peanuts) 459
- Theriot, Jackie, sugarcane farmer, Catahoula, LA; testifying on behalf of the American Sugar Cane League of the U.S.A., Inc., Breaux Bridge, LA 461
- Kline, Lloyd, cotton farmer, Lamesa, TX 465
- Wilson, Jimmy L., cattle rancher, Trout Creek, MT 472
- Gardner, Bruce L., Assistant Secretary for Economics, U.S. Department of Agriculture, Washington, DC 479
  - Prepared statement 483
  - Table 1—Cost of Production Estimates 494
  - Charts 495
  - Tables:
    - U.S. corn production costs and returns per planted acre, 1986–88 500
    - U.S. cotton production costs and returns per planted acre, 1986–88 501
    - U.S. rice production costs and returns per planted acre, 1986–88 502
    - U.S. soybean production costs and returns per planted acre, 1986–88 503
    - U.S. wheat production costs and returns per planted acre, 1986–88 504
- Sanner, Harvey Joe, soybean farmer, Des Arc, AR 507
  - Prepared statement 511
  - Costs of Production—Major Field Crops, 1988, Economic Indicators of the Farm Sector, Economic Research Service, U.S. Department of Agriculture, ECIFS 8-4, miscellaneous tables pertaining to production costs and returns of barley, corn, cotton, flaxseed, oats, peanut, rice, grain sorghum, soybean, sugar beet, sugarcane, sunflower, and wheat 516
  - Appendix table 1—Indexes of prices paid by farmers, 1985–88 524
  - FAPRI—1990 U.S. Agricultural Outlook, Staff Report No. 1-90, March 1990, Food and Agricultural Policy Research Institute, Iowa State University, University of Missouri-Columbia 525
- Felty, Wiley D., wheat farmer, Altus, OK 530
- Miles, Billy Joe, fertilizer retailer, Owensboro, KY 534

APPENDIX

Page

Waller, Helen, Agriculture Policy Committee Chair, National Family Farm Coalition, Washington, DC, prepared statement 551
  Family Farm Act 1990, submitted by the National Family Farm Coalition 554
Heagler, Dr. Arthur M., Associate Professor, Department of Agricultural Economics and Agribusiness, Louisiana Agricultural Experiment Station, L.S.U. Agricultural Center, and Dr. J.A. Musick, Professor and Resident Director, Rice Research Station, Louisiana Agricultural Experiment Station, L.S.U. Agricultural Center, prepared statement 561
  Tables 1-4, comparison of estimates of rice costs of production and returns 562

PREPARATION FOR THE 1990 FARM BILL

Crop Insurance

TUESDAY, MARCH 6, 1990

U.S. Senate,
Subcommittee on Agricultural Production and
Stabilization of Prices of the
Committee on Agriculture, Nutrition, and Forestry,
Washington, DC.

The subcommittee met, pursuant to notice, at 2:10 p.m., in room SR-332, Russell Senate Office Building, Hon. David H. Pryor (chairman of the subcommittee) presiding.

Present or submitting a statement: Senators Pryor, Harkin, Conrad, Baucus, Kerrey, Cochran, Boschwitz, and Bond.

STATEMENT OF HON. DAVID H. PRYOR, A U.S. SENATOR FROM ARKANSAS

Senator Pryor. Good afternoon, ladies and gentlemen. Our subcommittee will come to order.

We come to this table this afternoon in search of ideas and direction, in hopes of defining a suitable means of risk management for America's farmers. The simple mention of this subject usually triggers an immediate warning signal to most, as this has become one of the least agreeable issues we are to address in the 1990 farm bill. I, for one, am not sure that Congress has time to craft a responsible and well-serving piece of legislation that can be included in the farm bill; when faced with the alternatives, however, we should feel compelled to develop a form of crop insurance that will serve farmers according to need, and one that is within the bounds of budget realities—much easier said than done.

Today, I think, should serve as sort of a litmus test for all of us involved. The time for posturing, I think, is over; the time for genuine ideas and cooperation is here, and it is here upon us. Much has been said during the past several months, but there is one fact worth repeating, and once again worth emphasizing: the farmer is the one we are here to serve; the rest is merely in periphery.

We cannot ignore the sobriety offered by today's budget constraints, yet we are equally bound, I think, to devise a plan that is policy driven, based on the individual farmer's need. If we are to ever realistically increase participation in a risk management program, it will be done with a program that farmers approve of, because it serves them well, not because it has been mandated.

Today we are holding this hearing because there is much disappointment with the current program. That is no secret. That comes as no surprise. Just under 40 percent of eligible cropland was covered in 1989, and remember, this follows mandatory participation resulting from the past two disaster bills. In Arkansas, barely somewhere in the neighborhood of 17 percent of our eligible acres were protected by crop insurance. Yield guarantees for soybeans, for example, in the 13 Southeastern States have been reduced 35 percent since 1987. A new farmer in Arkansas, or a farmer on new land, can be covered a maximum of 7.5 bushels of beans an acre. Atrocities such as these leave very little doubt in our minds as to why farmers are not overjoyed with the present situation.

While the program is less than satisfactory, the administration of it has been arguably worse. If the administration's proposal for planting flexibility is adopted, farmers would clearly be in a higher risk venture. Under that proposal, more than any other, the farmer will need a dependable crop insurance program. If the farmer is to be encouraged to head in the direction of unlimited flexibility, then those offering the encouragement should also offer a worthy program that will help individual farmers manage their risks today.

The subcommittee welcomes each of you today, all of our participants and all of our witnesses, and we look forward to today's testimony.

Senator Mikulski, I know that you are first up. I understand that Senator Baucus is here. He is now managing the clean air bill on the floor. I will at this time call on Senator Baucus, and then our friend, Senator Mikulski.

Senator MIKULSKI. I would be happy to yield to the chairman of the Senate Subcommittee on Environmental Protection. We know his duties are most pressing.

Senator PRYOR. He has a full plate on the Senate floor.

Senator MIKULSKI. Absolutely.

Senator PRYOR. Thank you, Senator Mikulski. Senator Baucus.

STATEMENT OF HON. MAX BAUCUS, A U.S. SENATOR FROM MONTANA

Senator BAUCUS. Mr. Chairman and Senator, I very much appreciate your yielding. I will be very brief. I wish I could be here for the entire hearing.

Federal crop insurance is critical to my State. Even though the average participation rate nationwide has been relatively low, in Montana it has been very high. The percentages are in the neighborhood of 60 to 70 percent participation rate in my State of Montana. And that is because we need Federal crop insurance.

Now, I admit there have been some problems with the program. Farmers are concerned about high premiums and low coverage. They are concerned also about too much paperwork. But it is critically clear that we should not adopt the President's recommendation, which would cancel Federal crop insurance and resort to a disaster assistance approach to aid farmers. The administration's proposal is an anathema to individual farmers.

Some counties may be declared disaster areas. Some counties may not. Some farmers may be hit in an individual part of a county, whereas other counties may not be hit with hail or other bad weather conditions. So, I strongly urge the committee to press vigorously for a very strong, effective Federal crop insurance program.

[The prepared statement of Senator Baucus follows:]

PREPARED STATEMENT OF HON. MAX BAUCUS, A U.S. SENATOR FROM MONTANA

Thank you Mr. Chairman for holding this hearing today on Federal crop insurance.

Federally supported crop insurance has existed in various forms since just after World War II.

But the current comprehensive program was created in the Federal Crop Insurance Act of 1980.

The purpose of the 1980 act was to greatly expand availability of Federal crop insurance and to eliminate the need for disaster relief legislation for farmers.

As we all know, the current program has not accomplished this objective.

In most parts of the country, participation has been low. In 1988, only about 26 percent of eligible acreage was enrolled.

In addition, Congress found it necessary to pass relief legislation in 1988, and again in 1989.

Major complaints I have heard from Montanans about this program are that:

(1) Premiums are too high;
(2) Coverage is too low; and
(3) There's too much paperwork.

But no one in Montana has ever told me they think we should do away with the crop insurance program.

Instead, they think it needs to be revamped to make it more attractive for farmers to purchase.

Montanans strongly oppose the administration's proposal to eliminate crop insurance and replace it with a disaster relief program.

They want to be able to manage their own individual risk and not to be forced to rely on a government program to declare a county-wide disaster before they get relief.

In my view, the administration's proposal is a disaster in itself.

I think we in the committee can put together a crop insurance package that will solve the problems of the current program.

I look forward to working with the chairman and other members to put such a package together.

Retention of a crop insurance program is critical to any farmer who farms in the West.

Senator PRYOR. Thank you, Senator Baucus. Senator Conrad, do you have an opening statement?

Senator CONRAD. I do have a rather lengthy opening statement, Mr. Chairman. It is probably 50 or 55 minutes in length.

Senator PRYOR. Well, we look forward to putting that in the record.

Senator CONRAD. I thought you might.

Senator PRYOR. No, whatever you wish.

Senator CONRAD. Let me just thank you for having this hearing. It is terribly important to my State, yours as well, and I will not impinge on our time. I do have a statement that we will just submit for the record.

Senator PRYOR. Thank you, Senator Conrad.

[The prepared statement of Senator Conrad follows:]

PREPARED STATEMENT OF HON. KENT CONRAD, A U.S. SENATOR FROM NORTH DAKOTA

The debate over revising or replacing the crop insurance program promises to be one of the most contentious issues involved with putting together an effective and efficient farm bill in 1990. At one end of the debate, the administration proposes replacing crop insurance with a standing disaster assistance program that pays producers in the event of county-wide catastrophic losses. At the other end, there have been proposals to provide free crop insurance to all program crop producers that are afflicted with crop losses of 50 percent or more.

Most observers agree that the method of providing disaster assistance in the 1980's—which combined crop insurance, low interest emergency loans, and ad hoc disaster assistance programs—failed to provide assistance efficiently to needy farmers. But few have been able to suggest alternative strategies that provide adequate coverage for all farmers and are economically viable.

Farmers in my State of North Dakota have experienced severe droughts in 1988 and 1989. And this year, winter snowfall and spring rains have been sparse. The forecast for a third year of drought is again high for North Dakota. Crop insurance, emergency loans, and disaster assistance have all been extremely important to the North Dakota farmer as well as to the rural towns and communities.

Most of the North Dakota farmers use Federal crop insurance as an integral part of their risk management plan each year. North Dakotans insured 89 percent of insurable acres in 1989, for a total of 17,800,000 acres, primarily on 16 major crops. There were still some important crops not eligible for crop insurance. Clearly, North Dakota farmers would like to see greater flexibility and sound improvements in the crop insurance program, rather than elimination of the program as proposed by the administration.

Major policy debates require a common understanding of the situation before solutions can be found. Unfortunately, there are at least four misunderstandings that some people have about disaster assistance, and crop insurance in particular, that cloud the issue. These misunderstandings must be overcome before viable policy options can be explored.

(1) Crop insurance was the primary method of providing disaster assistance in the 1980's.

Congress revised the crop insurance program in 1980 to make it the primary method of providing disaster assistance to farmers. Nevertheless, the Federal Government actually spent less during the decade on crop insurance than other forms of disaster relief. Between 1980 and 1989, the Government spent $17.6 billion on disaster assistance, with less than 25 percent ($4.3 billion) going to support crop insurance. Nearly $7 billion was spent on ad hoc disaster payments (including $4 billion in 1988) and almost as much ($6.4 billion) was spent on emergency loans. During the decade, the Government spent virtually the same amount on emergency loan interest subsidies as it did on the entire crop insurance program.

(2) Crop insurance participation rates are too low.

Congress established a goal of 50 percent participation when it reformed the crop insurance program in 1980. This goal has not been met. Even with mandatory participation for those receiving assistance under the Disaster Assistance Act of 1988, less than 45 percent of eligible planted acres were covered by crop insurance in 1989. Prior to 1988, when it was voluntary, national participation peaked at 25 percent. Some farmers have rejected the crop insurance program as being inadequate, complicated, and expensive.

However, from a program point of view, achieving a 50 percent participation rate every year may not be practical or desirable. Because crop insurance is only one of many ways farmers manage their production risks and farm income, it is difficult to tell when participation rates are high enough. It is also unfair to judge a program's success by its failure to meet an arbitrary participation rate, when there is no empirical evidence to demonstrate what that number should be. Instead, Congress must look at ways to improve the program so that farmers will want to participate.

(3) The crop insurance program has failed.

Although coverage and participation have increased throughout the decade, the crop insurance program has been considered a failure by some because of poor management and services, fraud and abuses, and poor financial performance. However, I would submit that the program cannot be labeled a failure, when it has not been given an opportunity to succeed for three reasons:

First, crop insurance has had to compete with other Federal subsidies and provided service with no entry costs. What is astounding is that the Government has been competing against itself in this case.

Second, the Government has not run crop insurance like an insurance program, despite intentions in the 1980 act that the program be managed on a business-like basis. Only about one-half of the current program is properly rated, according to Federal Crop Insurance Corporation (FCIC) managers.

Third and most important, the 1980's turned out to be a dreadful time to test the effectiveness of any crop insurance program. Three major droughts occurred, making this the most disaster-prone decade since the 1930's. Any disaster assistance program, no matter how well conceived, would have difficulty succeeding under these conditions.

(4) Crop insurance program can never succeed.

The 1980's disaster assistance experience indicates not that crop insurance has failed, but that it has not been given a chance to succeed. Many agree conceptually that crop insurance is a more effective and efficient way to deliver disaster assistance than disaster loans and ad hoc disaster payments. The Government Accounting Office (GAO) measured the performance of these three methods of providing assistance during the 1980's against eight policy criteria, and found that crop insurance satisfied more of the criteria than other programs. The Commission for the Improvement of the Federal Crop Insurance Program has not recommended elimination of the crop insurance program. Rather, the findings of the Commission are aimed at providing better and more cost-effective administration and operation of crop insurance for the Nation's farmers.

Given an understanding of the recent disaster assistance history and current economic situation of agriculture, North Dakota farmers are telling me that they need Federal crop insurance; and they want it improved. In my mind, it is clear that the one alternative that Congress should fully consider in the 1990 farm bill is the same one it chose in 1980—establish crop insurance as the primary approach for providing disaster assistance. However, we must set conditions that allow the program to function successfully. Crop insurance can be made to work in the 1990's.

Senator Pryor. We have a very distinguished guest at our committee table this afternoon, our colleague Barbara Mikulski, Senator from Maryland. And ever since, again I might say, ever since the first of the year every time I think that I have seen Senator Mikulski on or off the Senate floor, she always comes up to me and asks me when we are going to do something about Federal crop insurance. Senator Mikulski, we are proud that you are joining us this afternoon. We have a tough and thorny problem. We look forward to your statement and any suggestions you might render the subcommittee.

STATEMENT OF HON. BARBARA A. MIKULSKI, A U.S. SENATOR FROM MARYLAND

Senator Mikulski. Thank you very much, Mr. Chairman. I would like to ask unanimous consent that I submit my prepared testimony for the record and also a task force report developed by the Maryland Department of Agriculture.

Senator Pryor. Without objection, your statement will be placed in the record.

Senator Mikulski. Mr. Chairman, I am here today to speak really for Maryland farmers, and they are here in this room with me this afternoon as well as the Secretary of Agriculture for the State of Maryland. And this is really a new role for me because I am probably better known for my urban oriented legislation. But one of the great joys I have had at representing the entire State was to get out there and meet the men and women who live off the land and live off of the water, to meet Maryland farmers and Maryland watermen, to be with them in their homes and in their church halls and in the fire halls and listen to their day-to-day needs has been, indeed, very gratifying and a learning experience.

But it seems that every time I want to really talk to a farmer, it is because, the Government has created a problem. The Government now is a bigger problem for the farmer than what they used to cope with. They get down on their knees and say their prayers every night to protect themselves against weather which could be an act of God, against pestilence, which could also be an act of God, and then they say a prayer to protect them from the U.S. Government which sometimes it is an act of—well, we are not exactly doing the Lord's work. [Laughter.]

Well, Mr. Chairman, we were hit by drought as was the rest of the country, maybe not as severely, but if you are hit by drought, it does not matter if you are the most severe. It has been severe for you. And when I went out to talk to the farmers and I asked about crop insurance, I found out that for Maryland farmers, only 5 percent of them, with only a mere 3 percent of eligible acres, were covered by the Federal crop insurance. Mr. Chairman, in short, Federal crop insurance to Maryland farmers is not worth warm spit off into the Chesapeake Bay in the midst of a traffic backup while getting over the Bay.

Now, Mr. Chairman, I claim no expertise in Federal crop insurance. So I asked the people who were the most affected to tell me the things to do and asked Wayne Cawley, our Secretary of Agriculture, to put the Report on Federal Crop Insurance together for me. They pulled together a task force for me made up of farmers, insurers, conservationists, and some of the agency folks. And Mr. Chairman, they came up with some very specific ideas, and that is what I just want to bring to your attention today.

Mr. Chairman, essentially what they said to me is:

Farmers cannot buy enough protection; the maximum available coverage is 75 percent of expected yield, and commodity price caps are set too low.

It is difficult for farmers to get information about insurance and find agents who sell it, and any information that is reliable and consistent.

Also, they find that the methods used to calculate insurable yields penalize some of the farmers.

Current crop insurance practices penalize farmers who either irrigate or operate several different farms as a single unit.

Farmers often find paperwork and recordkeeping excessive and onerous.

Some Maryland crops, like cabbage and cantaloupes, are not eligible for coverage.

The task force came up with essentially 8 short-term policy changes and 10 long-term. Let me just go through them.

Short-term, adjust price selection; make assigned yields higher; make crop insurance information available at the ASCS county offices; have private companies provide agent lists to the FCIC so you don't have to spend all day on the phone trying to find out even where to go and who to talk to; changes in overall policy should be made on a more timely basis throughout the system; and make the ASCS and the FCIC use the same yield methods. You have two government agencies each using different yield methods, and the farmer trying to figure out what to do. And also make it easier to separate irrigated units within a farm.

Those are right now that we could do.

Then there is the long-term recommendations that would require legislative changes to the Crop Insurance Act of 1980: Allow farmers to designate separate units for farms combined under the same farm ID number; current price election system should be modified or deleted; have the ASCS act as a crop insurance information center and sales agent. Let us have a one-stop shop for the farmer, a one-stop shop for the farmer where they get all of the information they need, and that that information is reliable and consistent. And that also means we have to train and certify crop insurance agents. The information is uneven. Most insurance agents are reputable people. Many of them have State licensing, but you call three insurance agents, and you are going to get five opinions, and when you go back to ASCS you are going to get seven other comments. And for the farmer that is just too much to put into any given day. Also, revamp compensation agreements to provide agents a finder's fee when the ASCS writes a crop insurance policy; and then for the agricultural program, maintain all crop records for both agencies; conduct yield-loss appraisals, and let the ASCS pay claims on FCIC proposals.

Mr. Chairman, in sum, that is what my task force did for me. It is simple. It is straightforward. It is as common sense as the Maryland farmers and the team who helped write it. And Mr. Chairman, I think if we adopt it, both these short-range and long-range procedures, we would have revamped the crop insurance program.

Let me conclude by saying Senator Baucus' comments were right as were yours. Crop insurance right now is like a bad back. It does not need orthopedic surgery. What it needs is a good chiropractor who pokes it in line with what needs to be done. And I think if we take this common sense approach, recommended, I know, by other farmers around this country, we will be able to do something. And Mr. Chairman, I would like to just let you know that the Maryland folks who are here—because I am real proud of them—I mean I did not know a soybean from a jelly bean when I came to this Senate. [Laughter.]

I now know it. The best thing I did for the Maryland farmer was to be a good eater, and I continue to do that. But we have Wayne Cawley; his son Charlie, the task force chairman; Hank Spies of the Soybean Association; Steve Connelly; Alice Beattie; Dr. Chambers; Alan Brauer; Jim Richardson and Royden Powell. Mr. Chairman, that is my testimony, but know that it is not me sitting here. It is really the Maryland farmer. So that concludes my testimony, and I will be happy to answer any questions you might have.

Senator PRYOR. Senator Mikulski, this has been a breath of fresh air for this subcommittee this afternoon to have you here, and I will tell all the good farmers and those representing agriculture from the State of Maryland that we have a saying in the Senate that if you have an issue out there, we want Barbara Mikulski on our side. We do not want her against us. And she is on your side. And literally all year she has been asking me not only about this hearing, but some of the things that we can do in a common way to help support some type of Federal crop insurance program that is not only fair but is affordable. And we really appreciate very much, Senator Mikulski, your being here this afternoon.

Senator MIKULSKI. Thank you, Mr. Chairman. If there are any questions?

Senator PRYOR. I would very much appreciate it, and I know the other committees would, if the report of the task force that you have formed, if we could place that task force report in the record at the appropriate point. I think that would be very constructive.

Senator MIKULSKI. Let me hand it to you personally.

Senator PRYOR. Thank you, Barbara.

Senator MIKULSKI. Look how nice and short it is. Is this not refreshing?

Senator PRYOR. I know it. It is wonderful. It represents common sense and thank you.

Senator Conrad, would you have any questions for Senator Mikulski or comments?

Senator CONRAD. Mr. Chairman, I share your feeling about our colleague, Senator Mikulski. I would like to see her on the Agriculture Committee because——

Senator PRYOR. She can have my place. [Laughter.]

Senator CONRAD [continuing]. We have a lot of fights on this committee, and it would be nice to have Barbara fighting by our side——

Senator PRYOR. That is right.

Senator CONRAD [continuing]. In this committee hearing room. We can count on her out on the floor. She has previously expressed an interest in this issue to me, and expressed her concern about the effect that the elimination of crop insurance would have on the Maryland farmer. I very much appreciate her initiative to pull together a group of individuals affected by this issue, who in their turn produced a very useful report. I want to commend Senator Mikulski for showing this initiative. You have demonstrated the best kind of service to constituents.

Senator MIKULSKI. Thank you very much. Thank you, Senator.

Senator PRYOR. Thank you, Senator Mikulski.

[The prepared statement of Senator Mikulski and the Report on Federal Crop Insurance follow:]

PREPARED STATEMENT OF HON. BARBARA A. MIKULSKI, A U.S. SENATOR FROM MARYLAND

Thank you Mr. Chairman. I am here today to ask this committee to consider my Crop Insurance Task Force's report, and the bill I've introduced based on that report (S. 739, Federal Crop Insurance Revitalization Act of 1989).

Maryland farmers were hit hard by droughts in 1980 and 1983, and then again in the 3 consecutive years from 1986 to 1988. No part of the State was spared the economic impact of these natural disasters. The cumulative impact on Maryland farmers of the 1986–88 droughts has been estimated at $300 million.

Prior to 1987, the U.S. Department of Agriculture could provide emergency disaster payments to farmers afflicted by drought. But the farm bill of 1985 brought disaster payments to an end at the end of 1986. That left Federal crop insurance as the only buffer between farmers and the economic disaster of crop failure (except for special, one-time disaster payments of the sort Congress authorized in 1988).

In Maryland, only about 5 percent of the farmers and a mere 3 percent of eligible acres are covered by the Federal crop insurance program. I asked the Maryland Department of Agriculture to undertake a study, with farmers and others involved, to identify why farmer participation is so low, what the Government was doing to help or hurt the farmers, and what we could do about it.

Maryland's Secretary of Agriculture, Wayne Cawley, appointed a task force to identify crop insurance problems and suggest ways to make the program more acceptable to Maryland farmers. Among the problems identified by the task force are the following:

- Farmers cannot buy enough protection; the maximum available coverage is 75 percent of expected yield, and commodity price caps are set too low.

- It is difficult for farmers to get information about insurance and find agents who sell it.
- The methods used to calculate insurable yields penalize some farmers.
- Current crop insurance practices penalize farmers who irrigate, or who operate several different farms as a single unit.
- Farmers often find paperwork and recordkeeping requirements excessive and onerous.
- Some Maryland crops (cabbage and cantaloupes, for example) are not eligible for coverage.

The task force came up with 8 short-term and 10 long-term recommendations to improve the Federal crop insurance program. I submit a copy of this report for the record. Based on these 18 recommendations, I created my own crop insurance bill which has three major components.

First, it requires the Federal Crop Insurance Corporation (FCIC) to take into account each individual States' crop prices, instead of often lower national-average prices, when determining crop value. It also allows farmers to exclude drought years when determining crop yields.

Secondly, my bill makes crop insurance information more accurate and reliable by requiring all insurance sales agents to be trained and certified by the FCIC. It will also require the FCIC to conduct periodic evaluation of insurance companies.

Finally, my bill makes the program information more easily available to farmers. Local Agricultural Stabilization and Conservation Service (ASCS) offices will act as information centers, so farmers will always know where they can get crop insurance information. These offices will keep updated lists of local crop insurance agents who have been trained and certified.

This bill can stimulate discussion on the Federal crop insurance problems. I hope that this bill and the underlying report are used by this committee in their review of the crop insurance program.

This underlying report was created by Maryland farmers and agricultural professionals. I am pleased that many of them are here today. I would like to acknowledge those members of the task force who were able to make it.

Wayne Cawley, Maryland's Secretary of Agriculture; Charlie Cawley, the Task Force Chairman; Hank Spies, Soybean Association president and farmer; Steve Connelly, Maryland Department of Agriculture; Alice Beattie, farmer, crop insurance holder; Dr. Robert Chambers, University of Maryland; Alan Brauer, State Grange; Jim Richardson, State ASCS Director; and Royden Powell, farmer.

I thank the task force for their excellent work, and I thank the Chair and the distinguished members of the committee for this opportunity to testify. I look forward to continued participation in this important issue.

10

Report On Federal Crop Insurance
To
Governor William Donald Schaefer

1632

Submitted By
The Maryland Department of Agriculture

Wayne A. Cawley, Jr., Secretary

EXECUTIVE SUMMARY

Maryland farmers were hard hit by droughts in 1980 and 1983, and then again in the three consecutive years from 1986 to 1988. No part of the state was spared the economic impact of these natural disasters. The cumulative impact on Maryland farmers of the 1986-88 droughts has been estimated at $300 million.

Prior to 1987, the U.S. Department of Agriculture could provide emergency disaster payments to farmers afflicted by drought. But the Farm Bill of 1985 brought disaster payments to an end at the end of 1986. That left federal crop insurance as the only buffer between farmers and the economic disaster of crop failure (except for special, one-time disaster payments of the sort Congress authorized in 1988).

In Maryland, only about 5 percent of farmers and a mere 3 percent of eligible acres are covered by the federal crop insurance program. During a Maryland Department of Agriculture briefing for the Maryland Congressional Delegation last summer, Sen. Barbara Mikulski asked the Department to undertake a study to discover why farmer participation is so low.

Secretary Wayne Cawley appointed a task force to identify crop insurance problems and suggest ways to make the program more acceptable to Maryland farmers. Among the problems identified by the task force are the following:

- Farmers cannot buy enough protection; the maximum available coverage is 75 percent of expected yield, and commodity price caps are set too low.
- It is difficult for farmers to get information about insurance and find agents who sell it.
- The methods used to calculate insurable yields penalize some farmers.
- Current crop insurance practices penalize farmers who irrigate, or who operate several different farms as a single unit.
- Farmers often find paperwork and record-keeping requirements excessive and onerous.
- Some Maryland crops (cabbages and cantelopes, for example) are not eligible for coverage.

The task force determined that the bottom line for Maryland farmers is that crop insurance provide adequate insurance coverage at affordable and cost-effective prices. The task force also noted, however, that farmers must be willing to pay for increased service. The group recommended that the following short-term policy changes be implemented before the 1989 growing season:

1. Adjust price election.
2. Make assigned yields higher.
3. Make crop insurance information available at ASCS county offices.
4. Have private companies provide agent lists to the FCIC.
5. Allow separate units for each farm I.D. number without penalty.
6. Changes in overall policy should be made on a more timely basis throughout the system.
7. Make the ASCS and the FCIC use the same yield methods.
8. Make it easier to separate irrigated units within a farm.

The following long-term recommendations would require legislative changes to the Crop Insurance Act of 1980:

1. Allow farmers to designate separate units for farms combined under the same farm I.D. number, regardless of rental agreements.
2. The current price election system should be modified or deleted.
3. Have the ASCS act as a crop insurance information center and sales agent.
4. Revamp compensation arrangements to provide agents a finder's fee when the ASCS writes a crop insurance policy.
5. The FCIC should train and certify all crop insurance agents.
6. Allow separate units for full-season soybeans, irrigated soybeans and double-crop soybeans.
7. Have the ASCS maintain all crop records for both agencies.
8. Have the ASCS conduct yield-loss appraisals.
9. Let the ASCS pay claims on FCIC policies.
10. Private insurance companies should be evaluated annually for financial stability, information accuracy, and integrity.

INTRODUCTION

Maryland farmers were hit hard by the droughts of 1980 and 1983, and then again in the three consecutive years of 1986, 1987, and 1988. No part of the state was spared the economic impact of these natural disasters. The cumulative cost to Maryland farmers of the 1986-88 droughts has been estimated at $300 million. The resulting economic disasters in Maryland's agricultural community highlighted both the importance and the shortcomings of federal crop insurance.

Crop insurance offers farmers a buffer against destructive weather, insect infestation, plant disease, and other unavoidable threats to their crops. It also gives the farmer a way to turn otherwise unpredictable, uncontrolled crop-loss costs into a predictable cost of the farming business. Despite these advantages, only about 5 percent of Maryland farmers and some 3 percent of the State's eligible farm acres are covered by the federal crop insurance program. Our task was to find out why, and to suggest ways to improve the sign-up rate.

Our committee was made up of individuals involved with crop insurance on all levels. This mix allowed us to examine the problem from several important points of view -- the farmer's, the insurer's, the conservationist's, and the state agricultural administrator's.

This paper outlines the problems we found in the current crop insurance system, and lists the changes we have suggested to improve that system. In some cases, the changes can be made administratively by the various organizations involved; other changes will require action by Congress to change crop insurance law. We want to make crop insurance work better for all concerned, and especially for farmers.

BACKGROUND

Congress created the government-owned Federal Crop Insurance Corporation (FCIC) in 1938 to set up a national system of crop insurance. For years, the FCIC operated a limited crop insurance program that worked in tandem with a disaster payment program run by the U.S. Department of Agriculture's Agricultural Stabilization and Conservation Service (ASCS). But Congress overhauled the operation at the beginning of this decade with the Federal Crop Insurance Act of 1980, which began to phase out disaster payments in favor of an expanded crop insurance system. The Farm Bill of 1985 terminated disaster payments at the end of 1986, with the exception of specially legislated payments such as those authorized by Congress during the 1988 drought.

Despite the phaseout of disaster payments, the crop insurance program has not attracted strong nationwide farmer participation. From 18.4 percent in 1984, participation climbed to only 27.6 percent in 1987, far short of the 50 percent Congress envisioned when it changed the law in 1980.

HOW CROP INSURANCE WORKS

Farmers must make two different choices when they buy crop insurance: yield level and commodity price. A farmer may insure his crop for 50 percent, 65 percent, or 75 percent of yield. If a farmer's harvest falls below the insured level due to natural conditions, the insurance pays the difference. Crop insurance yields are generally based on actual production history (APH), which gives greater credit to farmers with higher yields, and makes crop insurance more attractive to more-productive farmers.

The second choice is commodity price. In a process called "price election," the farmer chooses one of three different price levels for insurance payments on his crop. In the case of corn, for example, a farmer may insure his crop at $1.50 per bushel, $2.00 per bushel, or $2.60 per bushel. For both yield and price, higher levels mean higher premiums.

Premium rates vary throughout the nation to reflect differences in productivity and risk of loss. The federal government pays approximately 30 percent of a farmer's premium cost up to the 65-percent yield coverage level.

The 1980 Crop Insurance Act shifted most of the responsibility for delivering crop insurance to the private sector. The two basic delivery systems are reinsured companies, which handle about 85 percent of insurance sales, and master marketers. Reinsured companies are commercial insurance companies that handle all aspects of crop insurance on their own, including sales, service, and loss adjustment. The FCIC insures these companies against extraordinary operational and actuarial expense. Master marketers are private insurance companies or agencies that sell and service crop insurance policies for the FCIC. Under this system, the FCIC handles loss adjustments.

PROBLEMS

Our investigation turned up a number of reasons why Maryland farmers are reluctant to purchase crop insurance. These include: lack of sufficient coverage; difficulty in getting information about insurance and finding agents who sell it; flaws in the methods used to calculate insurable yields; built-in penalties against farmers who irrigate, or who operate several different farms as a single unit; excessive paperwork and record-keeping requirements; and the lack of coverage for all Maryland crops. A complete list of the committee's findings and recommendations follows:

PRICE ELECTION AND YIELD LEVEL

PROBLEM:

It is the consensus of most farmers that they cannot purchase a high enough level of protection.

There is no correlation between the available price or yield levels and a farmer's need to insure total variable costs. The highest available yield coverage will replace only 75 percent of a complete crop failure, which in effect amounts to a 25 percent deductible. Similarly, available commodity price levels are too low to adequately cover a farmer in the event of crop loss.

The price election needs to be maintained at a high enough level to insure farmers get adequate coverage -- $200-$260 per acre for corn under current economic conditions and $150-$200 per acre for soybeans under current econmic conditions.

Farmers need higher and more flexible insurance coverage that will enable them to cover total variable costs; our investigation indicates that they are willing to pay increased premiums for it.

SOLUTION:

a. Farmers' needs can be met by not allowing the price election to fall below a maintenance level, or about $2.65 a bushel for corn. For 1989, the highest price election for corn is $2.60 a bushel, which corrects for some of the deficiency but does not solve the problem. Soybeans have an optional, market-based price election that is geared to the average of the last five days in March of the Chicago Board of Trade November futures, with a minimum of $5.50 a bushel. This looks like a reasonable alternative if it can be adjusted on a regional basis.

b. Another alternative would be to do away the price election altogether and allow farmers to insure their crop based on their costs of production. This would allow farmers to tailor the insurance package to their needs. Of course, the cost would increase with coverage, and a cap or ceiling (adjusted by states) could be used. Any gross coverage amount should not be set in a dollar amount. An absolute dollar amount would not be safe from inflationary pressures on production costs. The farm cost-and-return survey from National Agricultural Statistics could be tied to the maximum insurable cost on a state-by-state basis. The coverage level could be increased from a maximum of 75 percent of yield up to 100 percent, which in effect would increase gross coverage. It would not have to be a fixed percentage. The farmer could choose the percentage on a sliding scale.

PROBLEM:

The National Average Price is used to set the price election, and the same price election is used throughout the United States. This results in a situation where the local cash price in some states is below or close to the price election, while in other states it is farther apart. Because the basis is different, some farmers can be profitable with lower yields where basis is high (Maryland and Delaware), while other areas have higher yields with lower prices (Nebraska, Illinois) where basis is low. Both geographic areas are profitable but for different reasons: one for yield, the other for price. The current price election system does not allow for basis differences.

SOLUTION:

Adjust the National Average Price for local basis differences. This can be done the same way the ASCS adjusts for basis in the loan-redemption-via-certificate program. This will help low-yield, high-price areas obtain higher insurance coverage.

YIELD CALCULATION

Actual Production History (APH) is the current method for establishing yields. It is based on a 10-year moving average of a farmer's actual production. As a starting point for farmers who do not have previous production, ASCS yields are used.

PROBLEM:

APH is generally a good method for establishing yields. But in Maryland, after three disaster years in a row, farmers realize there is a flaw. In years when there is a loss, the APH yields go down as much as 10 percent a year, or 30 percent in three years. This results in a significant drop in coverage below what is economically insurable.

SOLUTION:

a. To correct this problem, a floor yield could be established to prevent yields from going too low. A maximum percentage loss for any one year (e.g., 5 percent) may be another alternative. Alternatively, ASCS yield could be used in loss years, or it could form a safety net that APH yield could not go below. APH could be modified as a 15-year average with the two or three high and low years factored out.

b. A better solution would be not to factor loss years for APH when a county is declared a catastrophic disaster area. The ASCS now uses a 40 percent crop loss in a given county as a determining factor for recommending disaster status. However, this does not guarantee that the county will be declared a disaster area, and this may become a problem if the loss becomes individualized.

PROBLEM:

ASCS yields are used when a 10-year production history is unavailable for determining APH, but Maryland ASCS statistics do not include irrigated yields. This causes problems for farmers who irrigate. There is an FCIC appeals process to handle this anomaly, but few farmers seem to know about it, and the result is that many farmers who irrigate do not take out crop insurance.

Farmers who irrigate part of their crop encounter another problem. Since the premiums for crop insurance are based on yield and since yields differ between irrigated and non-irrigated fields, if a farmer wishes to buy insurance for a specific crop he must insure the entire crop. Consequently, it may not make sense economically for a farmer, who irrigates a portion of his crop, to buy insurance.

SOLUTION:

Farmers should be able to insure dryland crops and not be forced to insure the irrigated portion of their farms. It would also help if the Maryland ASCS would establish statewide irrigated yields. Farmers and agents need more information about how to establish irrigated yields through FCIC.

PROBLEM:

Farms vary greatly in terms of productivity because of yield potential and weather patterns. With the attrition of farmers, more farms are being combined under one ASCS farm serial number. This results in an operational farm unit with considerable yield variability. Under the current system, all farms consolidated under a single serial number are presumed to have the same yield. A farmer may sustain a total loss on one farm and not collect insurance because of production on other farms within the overall unit.

SOLUTION:

This could be corrected by maintaining yields by land tracts or original farms, instead of combining farms into one unit.

PROBLEM:

The FCIC requires that all a farmer's farms be combined under one policy, regardless of farm I.D. numbers. At the same time, a farmer has the option of calculating his losses either in the aggregate, on the basis of all his properties, or separately by individual property. If the farmer chooses the individual property method, however, he is charged an additional 10 percent premium. This was done not for farmers, but to reduce the risk of loss to insurance companies and the U.S. Department of Agriculture.

SOLUTION:

Farmers should be allowed to maintain separate units as they choose, without being penalized.

PROBLEM:

The APH yield method is too complicated for some farmers. Not all farmers keep sufficiently detailed records, and many don't want to be bothered with the complicated process necessary to determine the APH.

SOLUTION:

Provide a dual-yield election. Farmers could choose to use their ASCS yield from year to year, or elect the APH process. This would satisfy both the better operators with higher yields and those who don't want to be bothered with APH. But this must not be a shield for inefficient farmers. If a farmer used the ASCS yield and consistently showed losses, the local ASCS committee would have to lower his yield.

PROBLEM:

Losses are calculated on loss for an entire crop within a given farm I.D. number, except where irrigated production is a separate unit from dryland. If a farmer has a total loss on part of the unit and normal yields on the rest, he will probably not have a claim. An example would be a field fire or hail, where one field would be totally destroyed but not the rest.

SOLUTION:

a. Calculate the loss on smaller unit sizes, such as fields or tracts.

b. Pay claims on the actual area involved when fire or hail cause the loss. The farmer would receive a total loss only on the affected area, while the rest of the unit's yield would be normal.

PROBLEM:

Within a given unit, soybeans are treated as the same crop unless they are planted after a predetermined cut-off date, in which case a late-planted agreement may be used. Problems arise when full-season soybeans and double-crop soybeans are planted on the same farm. Weather patterns, insects, or variety differences may cause one crop to fail while the other is unaffected, but both crops are treated as one for loss calculations.

SOLUTION:

Full-season and double-crop soybeans should be treated as separate units.

PROBLEM:

Farmers who irrigate have the same cut-off date as dryland farmers, even though the irrigators can still successfully grow a crop.

SOLUTION:

Farmers who irrigate need different planting cut-off dates, especially where double-crop soybeans are involved. A separate unit classification should be allowed in this situation.

PROBLEM:

The cost of irrigated coverage is high compared to dryland, especially considering that irrigated farming reduces the risk of loss.

SOLUTION:

Farmers who irrigate should be charged considerably lower premiums. However, there must be some guidelines to define adequate irrigation. Areas that should be considered include the type of irrigation, the area covered, the water source pump, capacity, and management intensity. This should be addressed when yields are being assigned to first-time insurers.

PROBLEM:

Farms with low ASCS yields will not be insured, because it is uneconomical to do so. This is especially true of a farm that is considered to be "new" for insurance purposes.

SOLUTION:

New farms should be assigned realistic county-average yields for corn and soybeans.

AVAILABILITY

PROBLEM:

Insurance is not available for all crops.

SOLUTION:

An insurance program should be developed for all Maryland crops (for example, cabbages and cantelopes).

PROBLEM:

Many farmers do not know where to get good information about crop insurance, and this problem is complicated by the dual delivery system. Because private insurance companies will not let the FCIC know who their agents are, there is no list of insurance agencies that sell crop insurance.

SOLUTION:

a. Private insurance companies should be required to provide the FCIC a list of all crop insurance agents. In turn, the FCIC would advertise where farmers could obtain information and purchase insurance.

b. ASCS county offices should be used as information centers, and possibly as sales agents as well. Private agents would still sell insurance, but it would also be available through ASCS offices. In counties with less than $5,000 in annual crop insurance premium sales, ASCS county offices should be the exclusive sales center.

PROBLEM:

In many areas, insurance and information are not available because of low profit margins to agents. Private agents will not sell insurance on low-volume and low-commission crops because of the amount of time and money involved.

SOLUTION:

a. Increase private agent commissions.

b. Merge similar FCIC functions into the ASCS. This would consolidate overlapping functions and yield-loss estimating. The FCIC currently relies on the ASCS for acre reports and I.D. locations. ASCS computers would handle yield-history information, and local ASCS offices would handle claims estimating and payouts. The reduction in the duplication of ASCS and FCIC functions would benefit the system.

CONCLUSION

Crop insurance must meet farmers' needs. Coverage must shield farmers from insurmountable losses. This is particularly important in light of the fact that agriculture has become a mature industry, with low rates of return. Insurance policies and timely and accurate information about crop insurance must be readily available on the local level. Crop insurance must be affordable and cost effective. However, farmers must be willing to pay for increased service. Flexibility and cooperation will be the keys to making crop insurance successful in Maryland.

We realize that there are some policy changes that could be implemented by the 1989 growing season. These are short-term recommendations:

1. Adjust price election.
2. Make assigned yields higher.
3. Make crop insurance information available at ASCS county offices.
4. Have private companies provide agent lists to the FCIC.
5. Allow separate units for each farm I.D. number without penalty.
6. Changes in overall policy should be made on a more timely basis throughout the system.
7. Make the ASCS and the FCIC use the same yield methods.
8. Make it easier to separate irrigated units within a farm.

The following long-term recommendations will require legislative changes to the Crop Insurance Act of 1980:

1. Allow farmers to designate separate units for farms combined under the same farm I.D. number, regardless of rental agreements.

2. The current price election system should be modified or deleted.

3. Have the ASCS act as a crop insurance information center and sales agent.

4. Revamp compensation arrangements to provide agents a finder's fee when the ASCS writes a crop insurance policy.

5. The FCIC should train and certify all crop insurance agents.

6. Allow separate units for full-season soybeans, irrigated soybeans and double-crop soybeans.

7. Have the ASCS maintain all crop records for both agencies.

8. Have the ASCS conduct yield-loss appraisals.

9. Let the ASCS pay claims on FCIC policies.

10. Private insurance companies should be evaluated annually for financial stability, information accuracy, and integrity.

The committee discussed the advisability of having the State of Maryland help subsidize crop insurance for the State's farmers. It is recommended that current crop insurance problems be corrected before this option is considered.

If the recommendations the committee has laid out are followed, participation in the crop insurance program will increase. Cooperation by the FCIC, the ASCS, the Maryland Department of Agriculture, the Cooperative Extension Service, and local crop insurance agents should provide Maryland farmers with the most efficient means of insuring their crops.

Senator **Pryor**. We are now going to hear from the U.S. Department of Agriculture, Mr. Jon Kislak. Jon, would you please come forward. You can sit at that end if you would like or you can come closer. I do not know how many members we are going to have this afternoon.

Senator **Conrad**. Mr. Chairman, if I might be permitted, I have a 2:30 meeting. There are two points I would like to mention before I must leave for my meeting.

Senator **Pryor**. Certainly. You have the floor.

STATEMENT OF HON. KENT CONRAD, A U.S. SENATOR FROM NORTH DAKOTA

Senator **Conrad**. As you know, the President's proposal suggests that we eliminate crop insurance and have a disaster program that would operate only if there was a disaster county-wide. Our State's Congressman and I just finished a series of farm forums across the State of North Dakota, where farmers informed us that uniformly they reject the President's proposal. They stated that if such a program had been in place during the droughts of 1988 and 1989, North Dakota's farmers would have been in serious trouble. Although there were many counties that did not qualify for a county-wide disaster, individual farmers in those counties experienced a disaster.

Under the President's proposal, there would have been no crop insurance, and they would not have qualified for the disaster program since it was not county-wide. Mr. Chairman, this is a matter that requires our attention.

The second point I would like to make regards the use of historic production as the basis for recovery. I do not believe that historic acres provide a useful basis for disaster payment decisions. The suggestion that we go from 10 years to 5 years makes the basis even more problematic. Say a farmer has had 4 bad years out of the 10, and in order to determine his/her disaster payments, the Government throws out high and low years. He will find that he is getting very little coverage under this program.

If you would move to a 5-year program, you would find that problem exacerbated.

Mr. Chairman, coming from a State that has been the most adversely affected by drought in the last 2 years, with great possibility for a third year of drought, I am well aware of the importance of a crop insurance system that works for our producers. They need to be able to ensure their risks just like any other business person. And a final note: the suggestion that we should model our crop insurance program after hail insurance programs where farmers insure on a dollars' per acre basis is a good idea. Why not be able to insure up to a certain dollar amount with a set premium and of course, some limitations? We cannot expect to insure wheat for some outlandish number.

But, let the farmer decide how much risk he or she is going to assume and let us have a crop insurance system that fits the needs of our producers. That is fundamental. We heard that consistently in my State during our recent farm forums. I hope together we can arrive at a solution.[1]

Senator PRYOR. Good. Thank you, Senator Conrad. Senator Kerrey.

Senator KERREY. I will just wait.

Senator PRYOR. Senator Kerrey is going to wait. Mr. Kislak (Jon), we look forward to your statement. Would you like to put the full body of your statement in the record and summarize, or do you need to read it all?

Mr. KISLAK. Senator, if it is satisfactory to you, we can just put the full body of the statement in the record, and let me summarize briefly if I may.

Senator PRYOR. Right. Your full statement will be placed in the record, Jon.

Mr. KISLAK. Thank you, Senator, and I appreciate the opportunity to sit up here instead of at the other end. Sometimes the gulf between us is too large anyway.

Senator PRYOR. Thank you.

STATEMENT OF JONATHAN I. KISLAK, DEPUTY UNDER SECRETARY, U.S. DEPARTMENT OF AGRICULTURE, WASHINGTON, DC

Mr. KISLAK. There is no reason to symbolize that.

Mr. Chairman and members of the subcommittee, I appreciate the opportunity to visit with you today. I think that we are all in agreement that we have to find a way to protect the American farmer. We have to find a way to protect rural economies with a safety net against catastrophic losses. It is good public policy, and I think we are all in agreement on that.

CROP INSURANCE AS WE HAVE IT TODAY JUST IS NOT WORKING

Let me comment though that crop insurance as we have it today just is not working. It is not meeting the objectives set out in the 1980 crop insurance legislation. And given the budget realities, the administration just does not know how to fix the program so that it will be acceptable to producers and to taxpayers.

DISASTER ASSISTANCE OVER THE EIGHTIES HAVE AVERAGED OVER $1.1 BILLION A YEAR

The expenditures for crop insurance and for ad hoc disaster assistance over the eighties have averaged over $1.1 billion a year. Obviously, that is a lot of money for us not to be satisfied with the results. Producers, as you all have commented, are not satisfied with the product. Less than 45 percent of acres, eligible acres, were covered last year, and as you pointed out, Mr. Chairman, that is with a mandatory participation. In 1988 the participation peaked at 25 percent before it became mandatory.

THE INSURANCE INDUSTRY IS NOT SATISFIED

The insurance industry is not satisfied. The Commission for the Improvement of the Federal Crop Insurance Program that was appointed by Congress issued a 300 page report suggesting changes in the crop insurance program. These recommendations, although well-intended, would have cost hundreds of millions of dollars a year.

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[1] See p. 3–5 for the prepared statement of Senator Conrad.

A QUESTIONED RECOMMENDATION

One recommendation, in particular, Mr. Chairman, we would like to highlight is the question of the use of unadjusted ASCS yields as an alternative to proven yields. We estimate that that would increase the cost of the program by approximately 40 percent of the annual premium—it's a nice idea, but at the participation levels in 1989 it would have cost the Government over $300 million additional expense in the program.

THE AMERICAN TAXPAYER CANNOT BE SATISFIED WITH THE PROGRAM

Clearly, the American taxpayer cannot be satisfied with the program. We have a loss ratio from 1980 through the present of 1.58 percent. That means for every dollar including subsidy dollar of premium that we take in, we are paying out $1.58 of indemnity to farmers. This is not a program that is actuarially sound as was directed.

CONGRESS HAS SEEN THE NEED TO PASS AD HOC DISASTER LEGISLATION

Finally, Mr. Chairman, three times in the 1980's, really four times in the 1980's, in 1986, 1987, 1988 and 1989, Congress has seen the need to pass ad hoc disaster legislation. We have heard that the 1990 version of the disaster bill is already being discussed. In spite of more than $2 billion in premium and administrative subsidies, Mr. Chairman, the program still does not work.

SUMMARY OF THE PROPOSED PROGRAM

We have proposed a program, and I would like to summarize it briefly, to substitute. We are not sure how to fix the current crop insurance program within the budget realities, but we do not want to leave the American farmer without coverage from disasters which are beyond his control. Our program briefly is keyed by a disaster in a county area. It is keyed on a crop-by-crop basis to harvests of less than 65 percent of normal in that county. Payments would be based on 65 percent in one of those counties of the 3-year average market price for those farmers that harvested less than 60 percent in one of those counties.

The program is patterned after the 1988 and 1989 disaster legislation, and our intent was to try to adapt the parameters that were in those bills and to make a program that was compatible with the parameters in those bills. We believe, Mr. Chairman, that the program will end the need for ad hoc disaster legislation. It will be more reliable and predictable than ad hoc disaster legislation since the producer knows in advance what the parameters are. We believe that it will assist in better targeting disaster assistance dollars to areas that have catastrophic losses, and we believe that it will be less expensive to administer than the current crop insurance program.

While I was down in Florida earlier last month, Mr. Chairman, at the Crop Insurance Research Bureau, several members of the crop insurance community suggested that this program would allow them to go into a variety of privately offered, unsubsidized individual crop insurance programs. In fact, and I ask it be entered in the record, appended to my testimony is one unsolicited letter from Mr. Perry Rutledge, who is president of the Farmers Mutual Hail Insurance Company.[2] Mr. Rutledge is the largest writer of crop hail insurance in the Nation, has never participated in the Federal crop insurance program. He has suggested, as his letter says, that he is enthusiastic about the opportunities that will open to the private sector to write coverage if the Federal Government leaves the field. And he intends, as his letter suggests, to aggressively pursue a program of offering individual farmer coverage as a companion to his crop hail policy.

That is basically our program. It provides a safety net of protection to farmers, Mr. Chairman, and we think that it meets the four areas that any responsible program has to meet.

First of all, it provides protections to farmers and rural communities against the financial problems associated with catastrophic crop losses.

Second, it ends the pressure for ad hoc disaster assistance legislation.

Third, it provides the system which permits the private sector to offer individual farmers protection.

Fourth, it achieves it within realistic costs within the means of the current fiscal situation.

We invite anybody else to come forward with other alternatives that meet these criteria. We would look forward to working with anybody on any ideas that they may have. Mr. Chairman, I would be pleased to answer any questions.

Senator PRYOR. Yes, thank you, Mr. Kislak. I am looking, I am holding, and I will place the General Crop Insurance Regulations in the hearing record at the appropriate place a Federal Register Rules and Regulations, volume 55, No. 40, Wednesday, February 28, 1990.

[See p. 192 for the copy of above-described Federal Register document, 7 CFR Part 401, Amdt. No. 58; Doc. No. 7867S, General Crop Insurance Regulations, Federal Crop Insurance Corporation, USDA.]

Senator PRYOR. This interim rule basically states, if I saw this and I were a farmer, that the administration will propose that Federal crop insurance as we know it today be eliminated, and in addition, you have stated out there this message goes to the farmer. You say, Mr. Farmer, now let me say that Federal crop insurance has been eliminated. Congressional action on the budget proposal of any sort of additional or disaster payments would be necessary. This sent a lot of shock waves through the agricultural community. Were you aware that this would happen when you published this in the Federal Register?

Mr. KISLAK. Mr. Chairman, we reviewed a number of alternatives for how to carry the message to farmers. You all know and which we all know that if there are no funds in the budget, then the program is, then the liabilities of the Corporation cannot be honored. There is a clause already, for instance, in the CRP contract that states exactly that, that the obligations of the Government are subject to appropriation. We attempted in this to make sure that the farmers understand that although they are buying a policy, if Congress chooses not to enact legislation and not to enact a budget to back up the obligations, then the Crop Insurance Corporation will be unable to meet the obligations that the farmer might otherwise have thought he had entered into.

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[2] See p. 42 for the letter of Perry Rutledge.

Senator PRYOR. Has the Federal Government ever to your knowledge ever failed to appropriate the necessary funds for the Federal crop insurance program?

Mr. KISLAK. No, sir, not to the best of my knowledge.

Senator PRYOR. Have you ever run a notice like this before?

Mr. KISLAK. No, sir, we have not.

Senator PRYOR. Any reason for doing it now?

Mr. KISLAK. To the best of my knowledge, Senator, this is the first time that there is controversy about the program, that there is a proposal in the program to both eliminate the program and to not fund the obligations. Starting on March 1, we are starting to sell policies. Both our direct agents as well as the insurance industry are starting to sell crop policies for the 1991 year, 1991 crop-year, and this was aimed at making sure that farmers understood what was already the fact. This does not make a new regulation or a new law, in our opinion, but just make sure that farmers understand.

Senator PRYOR. You are saying it might be all right if you would like to buy some crop insurance for the 1991 crop. You are also saying but there might not be any money by the time you have any need to cash in or make a claim against that insurance; is that right?

Mr. KISLAK. What I think if I were a farmer, Senator, I would read into that is that as always, if Congress does not appropriate the funds, then there will not be funds to pay. At the same time, Mr. Chairman, the individual farmer would not be billed and would not have to pay his premiums.

Senator PRYOR. Senator Kerrey.

Senator KERREY. Well, Mr. Kislak, I guess it is substantially different than the CRP. In this case the administration is not making a recommendation to fund. It seems to me that your interim rule, at the very least, does not tell the entire story. In this particular instance, the administration is not recommending to fund. That does not hold with the CRP. With the CRP the administration is making a recommendation to fund. So the comparison to me just does not hold at all. If you are out there purchasing insurance, it is much different than holding a CRP contract.

If you hold a CRP contract you know that President Bush has recommended to fund the program, and it is very likely Congress will fund based upon that recommendation. In this particular case, you are putting out a notice saying President Bush has recommended no funding. And under the terms that Secretary Yeutter laid down, unless we can find the money someplace else, there will be no money. You must see there is a substantial difference in the message that goes to the producer with this notification compared to the CRP.

Mr. **Kislak**. Senator, I appreciate your point. Our concern was that farmers not be out there during this time believing that they have coverage when, in fact, absent action by Congress there is not coverage.

Senator **Kerrey**. Well, with all due respect, then, you should have put us on notification when you received the recommendations last June. It was leaked to the press that there was a likelihood of not funding the crop insurance program during our recess. That was the first time we had any notification at all that it might occur. We were asked during the recess what we thought about this particular proposal.

So at the very least, it seems to me, the administration has not been very forthcoming with what it believes ought to be done. Last year during work on the disaster legislation, we were put on the spot because we were supporting some additional appropriation for disaster relief, and the administration's position at that time was that you have to pick one or the other. Pick one or the other, the administration said. A lot of us would like to pick crop insurance. And now you are saying there is going to be neither one.

The conclusion now is rather than picking one or the other, the conclusion now is that we have neither to pick from. That is essentially the administration's recommendation.

Mr. **Kislak**. Well, I appreciate the Senator's comments. I think that we have struggled, Senator, mightily to try to find a program that meets the needs of the American farmer and does it within the confines of the budget. In all honesty, this is the best we can do. We would be glad to sit down with you and your staff and anybody else to try and find other alternatives and would provide as much assistance as we can in that respect, Senator.

Senator **Kerrey**. Do you understand the President's budget provides no money for disaster assistance?

Mr. **Kislak**. Yes, sir.

Senator **Kerrey**. Either for this proposal that you have or for crop insurance. There is zero money in there for either one.

Mr. **Kislak**. That is accurate.

Senator **Kerrey**. So are you saying that you want to sit down with us or do you want to sit down with the President? Who are you going to sit down with here?

Mr. **Kislak**. The budget supports the proposal that we have made. OMB advises us that the proposal that the President has made for a disaster protection bill will be scored at zero, that OMB does not budget for contingencies. A disaster is a contingency, and this proposal will be scored at zero so that the budget accurately supports the proposal that we have put forward.

Senator **Pryor**. Did OMB make this decision on Federal crop insurance?

Mr. **Kislak**. I am not sure I understand the question, Senator.

Senator **Pryor**. Did OMB make the decision not to go forward with the continuation of Federal crop insurance?

Mr. **Kislak**. The OMB and the Secretary had long discussions. It was a jointly made decision.

Senator **Pryor**. How much impact did OMB have on that decision? Is this a budget decision or is this an agriculture policy decision?

Mr. **Kislak**. Senator, I was not privy to all the negotiations so I cannot answer how much was OMB and how much was the Agriculture Department. I will tell you that this is not the best of all the possible solutions. It is the best of all possible solutions that we can find within the monetary constraints. If we had a couple of billion dollars a year, we would fix crop insurance and make it work. But we just do not believe that there is $2 billion a year to do that.

Senator **Pryor**. Senator Kerrey.

Senator **Kerrey**. Mr. Kislak, again to followup, you say that OMB will score all contingencies as zero?

Mr. **Kislak**. Senator, I cannot speak for OMB. My understanding on this program is that OMB considers this obligation a contingent obligation, and that under this program it will be scored at zero.

Senator **Kerrey**. So if we put a program together that provides $1 million per acre benefit, they will score it at zero because it is a contingency.

Mr. **Kislak**. I cannot, Mr. Kerrey, respond to that on OMB's behalf. All I can tell you is that they tell us that this program will be scored at zero because of its contingent nature.

Senator **Kerrey**. Well, then, let me run it back to what you just said to me. You just cited OMB, and then when I asked you a question, you said you can't speak for OMB. So you are speaking for OMB at least in this particular sense, that OMB will score at zero this proposal because it is a contingent liability.

Mr. **Kislak**. That is how they will score this proposal. That is my understanding, Senator.

Senator **Kerrey**. So it does not matter what we write in there for the reimbursement amount? They are going to continue to score it at zero?

Mr. **Kislak**. I cannot respond on OMB's behalf as to what point it becomes something that is noncontingent, and that they would have to score, Senator.

Senator **Kerrey**. I predict, Mr. Kislak, that they do not score it at zero; that they put a cost on it. As soon as we mark this bill up, as soon as we put any dollar figure for reimbursement in there, OMB will not score it at zero unless we mark zero for reimbursement. The administration is providing resources only if the mathematical number zero means something to you. That is what they are providing. You cannot hide behind this game that OMB scores a contingent liability at zero. It does not work because the minute I follow with a question as to what they would do if we provided $1 million an acre, you say, well, I cannot speak for OMB. You cannot have it both ways. It seems to me you have to say the administration is asking for zero for either the crop insurance or the disaster program. That is their recommendation.

Mr. **Kislak**. Senator, the program we have proposed, in the event that there is a contingency that requires funding, would get funded out of the CCC. It costs real dollars. At the outset of the budget, OMB advises us that this program requires zero reservation of funds, zero scoring. It would be reviewed at the midyear review, I understand. Based on the information that would be available at the time of midyear review, it would at that time get scored based on the information that was available at that period in time.

Senator **Pryor**. Senator Kerrey, thank you. Let me ask you a couple of questions about a decision made December 28, 1989, Federal Crop Insurance Corporation issued modifications for the 1990 soybean program in 13 Southeastern States. What this basically did was it reduced the yield guarantee in 13 of those States on soybean protection. Sixteen Members of this committee and of the U.S. Senate representing these States wrote to the U.S. Department of Agriculture, to the Secretary, asking why this had been done, and two, what was going to be done in the future if there was going to be any follow-on, and to give us an explanation of this decision.

We have received no answer to that. Are you familiar with this?

Mr. **Kislak**. Senator, I am not familiar with the letter. I am somewhat familiar with the situation in Southeast soybeans.

Senator **Pryor**. Well, USDA knew that this hearing was on the schedule. The Secretary knew that we were going to be here today for one purpose. We were going to be here to talk about Federal crop insurance. This letter and these questions posed is very, very critical and must be factored into any decision or any hearing that we have on Federal crop insurance. Now we are going to be looking for an answer to this letter, hopefully this week. This is Tuesday, and we need it this week, and I hope you will go back and stress the fact how critical this is.

Now my question might be what do you think, back to our Federal Register notice, what has this notice or is this notice going to do to participation in the Federal crop insurance program?

Mr. **Kislak**. Senator, to the best of my knowledge, it has not had any effect yet. We do not think that it will have a major change in participation. We think that the farmers who are buying crop insurance will be better informed.

Senator **Pryor**. And you think this little nifty cloud that you have hung over this new ruling, you are going to say—not new ruling—but you have said we just want to warn you there may not be any money for the claims if you file?

Mr. **Kislak**. It was not our intention, Senator.

Senator **Pryor**. That does not encourage the selling of many insurance policies.

Mr. **Kislak**. I understand your concern, Senator, it was not our intention to put any cloud over participation in the program. We intend to operate this program as an ongoing program until the day after the President signs any proposal, any bill that directs us differently. We do not intend to try and usurp congressional authority in this, and we intend to run the program as best we can, as if it is an ongoing program.

Senator **Pryor**. A moment ago Senator Conrad talked about meeting back in his home State of North Dakota lately, recently, said that farmers are worried about many things. I will tell you where I am beginning to get a lot of worry about the abolition of the Federal crop insurance program, and that is from rural bankers. Rural bankers today are wanting to know what is going to be done in the area of Federal crop insurance? Will there be a disaster program? What do they have to go by that they can look at that farmer when he comes into that bank and say that there is something that is going to make him and ultimately this bank whole in case of a disaster?

Now what am I supposed to tell those rural bankers back home, and what is Senator Conrad and Senator Kerrey and Senator Bond, back in Missouri, to tell his rural bankers?

Mr. KISLAK. Senator, we took a survey of 1988 participants in the crop insurance program, and remember, that was a very small group of farmers. That was only 25 percent of all acres to start with. Only 10 percent of those people went to private lenders who required crop insurance. That is a very small number. That would mean that in the neighborhood 2½ percent of farmers are buying crop insurance because their lender requires it. I wish that over the years lenders had required crop insurance more widely. We would not have a participation problem. But the facts just do not bear that out.

Senator PRYOR. I have one or two questions. Then we will let Senator Kerrey continue, and then we will call on our friend, Senator Bond, from Missouri. Mr. Kislak, have you ever actually been out in the field and tried to sell an insurance contract on soybeans?

Mr. KISLAK. No, sir.

Senator PRYOR. Well, I never have either, and I think both of us probably should. But I hear it is not very easy, especially in light of the decision made last December, which this letter pertains to, and also now with the idea that Federal crop insurance is going to be abolished, and the so-called veil warning that there may not be any money if there are any claims there. So I think for all practical purposes, at least for the money, for the moment, there is a strong likelihood that we are not going to see any activity in Federal crop insurance. Is that the purpose, is that the hope of the administration that you are trying to scare people out of buying a policy?

Mr. KISLAK. No, sir, not at all.

Senator PRYOR. Do you want them to buy private policies?

Mr. KISLAK. No, sir. Our intention, as I suggested before, is to run this program aggressively, as we have, and as aggressively as we can to bring farmers in until the day after there is legislation passed that changes the program and says to stop.

Senator PRYOR. Senator Kerrey.

Senator KERREY. Well, just for the record, I do not see evidence of the program being aggressively run at all. I really do not, Mr. Kislak, with all due respect, but I understand that you need to represent the contrary. I do not see it occurring. I see people in my State being required by lenders to purchase crop insurance to get loans. The 2½ percent figure you cite is not meaningful in the face of the evidence that I see out in the field. You have the recommendations made by the Crop Insurance Commission last June. You have implemented 3 out of the 26 recommendations. Your price elections have been inadequate to get people to purchase the insurance. It seems to me you have done everything humanly possible to make the program unattractive.

It seems to me you have done everything humanly possible to make the program fail, and now that it is not working very well, you are coming to us and saying, see, we were right all along. That is my attitude toward it, so you can factor that into your consideration. You mentioned this Mr. Rutledge, one of several people that you talked to. I think you would admit that one person is not a very scientific, not a very persuasive number. Does this Mr. Rutledge sell entirely hail insurance?

Mr. KISLAK. To the best of my knowledge, hail and fire insurance, yes, sir.

Senator KERREY. But as far as crop insurance goes, he is talking about hail?

Mr. KISLAK. Yes, sir, he does not and has never participated in the Federal crop insurance program.

Senator KERREY. You understand the significant difference between all risk and hail?

Mr. KISLAK. Yes, sir. Mr. Rutledge has not participated as a matter of his own policy. Mr. Rutledge, as I understand it, is by far the largest provider of hail policy in the country. He understands crop insurance as an industry. He has always said, as I understand it, and I have not been in the industry as long as he, that the Federal crop insurance program did not offer profit opportunities. It was not a business that he wanted to be in. He is excited by the possibility of the Federal Government stepping back and allowing him to offer policies in addition to hail and fire.

Senator KERREY. But you have selected somebody who is pretty hostile to the FCIC in the first place?

Mr. KISLAK. I have selected the man who is the largest provider of hail insurance in the country.

Senator KERREY. And somebody who does not like your program to begin with——

Mr. KISLAK. Yes, sir.

Senator KERREY [continuing]. To comment on the validity of your program? It is an interesting selection, I have to say.

Senator PRYOR. What about if you live in a region of the country that does not have any hail?

Mr. KISLAK. I am not sure I understand the question, Senator.

Senator PRYOR. Is he going to sell drought protection and other types of protection?

Mr. KISLAK. Senator, I assume that he and others who are of like mind who do not yet feel strong enough to stand up in the face of the PR barrage that certain members of the industry have put forward, that the private sector will offer policies all over the country. That this program that we have proposed gives them an umbrella underneath which they can write crop insurance and drought insurance and multiperil insurance. And that the private sector will come forth and offer policies all over the country. Whether Mr. Rutledge's company will or not I cannot testify.

Senator PRYOR. Well, we have some good questions for our upcoming panels on what they think of just the purely private insurance programs. Senator Kerrey, any further questions?

Senator KERREY. Yes. Can you tell me when you began to work on this particular program? What was the first meeting date when this disaster assistance program was discussed?

Mr. KISLAK. Senator, during the fall and early winter, the Department of Agriculture was working on alternatives. We came to this conclusion——

Senator KERREY. Can you be a bit more precise? Fall and early winter? What are we talking about there? Fall and early winter?

Mr. **Kislak**. We are talking about October, November, December. I think we presented an option paper in mid-December, maybe in November, but in that timeframe.

Senator **Kerrey**. Did that option paper include this disaster assistance program?

Mr. **Kislak**. It included a generic disaster assistance program. The finishing touches on this one were put forward probably around Christmas time.

Senator **Kerrey**. Did he in December then ask you to develop this disaster assistance program?

Mr. **Kislak**. Yes, sir.

Senator **Kerrey**. Did you in December contact any members of the Senate or the House Agriculture Committee to engage them in the development of this program?

Mr. **Kislak**. No, sir.

Senator **Kerrey**. I must tell you why I like the crop insurance program as opposed to a disaster program. A disaster program puts in the politicians' and the bureaucrats' hands, without using the word "bureaucrat" in a pejorative way, the assessment of risk. We design a program, and we try to equalize it and make it work for the whole country. We are making the decisions in Washington about how the program ought to work. It seems to me that where possible, we ought to say to the producer that you are the one who needs to manage the risk.

Your proposal seems to me to run in the opposite direction, and I must tell you it seems to me that it will cause the taxpayers in the end to spend an awful lot more money than they otherwise would. It is going to create additional Federal programs that will be administered out of Washington, D.C. rather than, as I said, having the producers make a choice. I must further comment that I am really disappointed that this program was developed very, very late. You say to me that you began work on it in December. You made no attempt to engage the Members of the Congress in the development of the program itself. And then you unveiled it. And I feel almost a pretense here, Mr. Kislak, because in the President's budget there is no money for this disaster program in spite of your assertion that OMB scores it at zero.

They did not score any programs that we submitted last year at zero. They will score this one just as soon as we put some numbers behind it and they will score it at significantly more than zero. You are asking us essentially to get the money out of the $10.2 billion that the President has provided for price support payments in 1991.

Senator **Pryor**. Thank you, Senator Kerrey. Senator Bond.

STATEMENT OF HON. CHRISTOPHER S. "KIT" BOND, A U.S. SENATOR FROM MISSOURI

Senator **Bond**. Thank you, Mr. Chairman.

Last August I had the pleasure of joining Senator Dole, Secretary Yeutter, and President Bush at the signing ceremony for the Disaster Assistance Act of 1989. This disaster legislation, the third in the past 4 years, signaled a worsening problem in American agriculture, the inability of the current system of Federal crop insurance, to provide our Nation's farmers with an adequate form of risk management. At the signing ceremony, President Bush indicated his desire to reverse the trend of providing both subsidized Federal crop insurance and ad hoc disaster assistance.

I agree with the President. We either devote the time to make crop insurance work or we replace it with a permanent disaster program. Let me emphasize one thing. Regardless of the route we take, I think the Federal Government must continue to provide producers with some form of risk management. Mr. Chairman, this committee has dealt with the problems in the Farm Credit System, and it was not easy to resolve those programs. As a result of a bipartisan compromise, I think we have been able to assure the continued availability of agricultural credit. And that measure, the Farm Credit Assistance Act of 1987, has worked well.

I would hope we could dust off that model of cooperation to develop a new system of Federal risk management. We are under a time constraint because this is a farm bill year. But I think we ought to devote the time that is necessary. In fact, I believe this issue will be one of the most time-consuming and complex ones that we will deal with during the farm bill. In January I wrote to Secretary Yeutter and expressed my dismay over the Federal crop insurance system. My letter stated I do not believe the current system can be modified to provide adequate, affordable coverage which eliminates the possibility of supplemental disaster assistance.

I came to this conclusion not on the basis of my own beliefs or the well-formed beliefs of people inside the beltway. I spent a good deal of time in Missouri talking to my Ag Advisory Committee broadly composed of leaders of variety of section of agriculture, a very diverse agriculture in Missouri, I might add. We discussed crop insurance. By and large, everyone there could point out substantial abuses in the system. I personally talked with people who sold crop insurance and they earnestly and eagerly pointed out to me that they had been able to gain coverage and payments for their clients in 85 to 90 percent of the cases in the last 2 years.

I asked them about the year prior to that which was a good growing year in Missouri. And they proudly stated that they were able to get payments for 40 to 50 percent of their clients in those years, too. Mr. Chairman, what kind of shell game are we running if this is designed to pay out in good years and bad? The farmers I have talked to said that, at least as we view it in Missouri, the incentives are wrong. Now after I came out with a statement that we ought to abolish FCIC and go with a permanent disaster assistance coupled with a form of insurance, an optional form of insurance, I have had several more hearings. As you might gather, I had some interesting reactions. At each one of the hearings, I encountered a representative of crop insurance, someone who sold crop insurance and was prepared to state his case.

In those meetings, however, that person was the only one who spoke up for crop insurance. Customarily one or two others would get up in the meeting and say they agreed it did not work. After the meeting was over, others would come up and volunteer their examples as to why it did not work. Obviously, that is not a scientific study, but it is the best way I can get feedback in my State on what is working in the country and what is not. I think the question is can we increase participation significantly; can we fix the system without corresponding increases in cost? I agree that there are some very interesting ideas. Unfortunately, it has very heavy price tag associated with it.

Also, I am afraid for some reason the incentives are not right. I am not sure it cures the problems that we see of payments in inappropriate times. If we look at the example, as I understand in Canada, we might be led to conclude that even if we were able to get a system of participation up to 75 percent, that 25 percent of the producers who were not covered would still be in a position to push Congress to pass a disaster relief act. So we once again have the dual system of subsidized insurance plus disaster relief. And I think we know only too well in this committee that disaster assistance for one crop suddenly becomes a several hundred crop assistance bill.

A few weeks ago when Secretary Yeutter appeared before the committee and outlined the administration's farm bill proposals, I was pleased to learn that the USDA shared my frustration with the FCIC, and I believe that we should have some kind of permanent disaster assistance. However, I have a concern which has been reflected to me by quite a few people from Missouri who are concerned that under the administration's proposal individual losses must be preceded by a county-disaster declaration. There is a concern that a localized disaster, and nothing is more specific in our part of the country that a tornado, would not be sufficient to trigger disaster relief. So we need to look at that side of it.

As we look at solutions, the idea that keeps popping up and keeps coming back to me from people in the heartland is to combine the best of crop insurance with a catastrophic disaster program. In other words, provide disaster assistance for losses exceeding, say, 75 percent and build that in permanently. What we have done in the 1988 and 1989 seem to be a good model, and then for losses between or below 75 percent, maybe down to 30 or 25 percent, there would be an availability coverage in private crop insurance. If needed to make the program work I think we could take some of the savings and use them as a partial subsidy for the premiums. But I really think the administration of it and the responsibility of bearing the loss in those years when losses are not truly the work of a natural disaster should be in the private sector.

Alternatively, and less desirably, we could have some type of fallback government insurance, but I believe my colleague from Nebraska has raised the question about whether, about how well we can design that system from Washington. I would prefer to see some kind of plan involving the private crop insurance, perhaps with a subsidized, if necessary, a subsidized component on the premium from a portion of the savings from eliminating crop insurance. Mr. Chairman, obviously, this is not going to be an easy subject. There are some very strongly held views here. I think we need to ensure that there is a risk management system in place. I hope that we would not be forced to continue a system where we subsidize an insurance system, and yet we still go back every year on an ad hoc disaster assistance program and wind up with a dual system which we do not really need.

I would only ask, Mr. Chairman, if I might, I would ask Mr. Kislak, what would be the impact of going with no county loss trigger? Or say, a lower county loss trigger? How could you deal with the situation of the tornado, for example, which is most frequently raised in my State?

Mr. KISLAK. Senator, it is our belief, and we have heard from some and not yet all of the industry, that tornadoes, similar to hail, similar to fire, can be covered, and, in fact, would be covered by private nonsubsidized policies tailor-made to your State or to Nebraska or to whatever State one was in. Those losses are noninterdependent losses. They are the kinds of things that are insurable in the private sector just as hail is insurable in the private sector, and we would anticipate that in an area where there was a substantial problem with tornadoes that the private sector would offer policies with protection against tornadoes. We would anticipate just as they do in areas where hail is a prevalent risk that the private sector offers hail policies without Federal involvement in those policies.

Senator BOND. A final question just on the logistics of change. For next year's crops, when do contracts need to be written, and are they likely to have to be written before Congress could expect to have the revisions made or scrap the program in favor of disaster assistance. What kind of timeframe are we looking at?

Mr. KISLAK. The contract change date for the first 1991 crop was February 28. That is the date by which there have to be changes to the contract. The sales closing date for the first 1991 crop is May 31? Is that right? It is May 31.

Senator BOND. This year?

Mr. KISLAK. This year for 1991 crops. Those apply to Texas citrus. Wheat, for instance, the first big program crop, has a June 30 contract change date and a September 30 close date. And that is the first program crop for the 1991 crop-year.

Senator BOND. OK. Thank you, Mr. Chairman.

Senator PRYOR. Did the administration feel that or assume that Congress would have the 1990 farm bill on the President's desk and signed at this time or before this?

Mr. KISLAK. No, sir, we all hope that we can finish it sooner rather than later, but I do not think we thought it would be done this quickly.

Senator PRYOR. Senator Kerrey.

Senator KERREY. I have no other questions.

Senator PRYOR. Thank you very much, Mr. Kislak.

[The prepared statement of Mr. Kislak and attachment A, letter of Perry Rutledge and article, "A New Kind of Crop Insurance" follow:]

TESTIMONY OF

JONATHAN I. KISLAK

DEPUTY UNDER SECRETARY

UNITED STATES DEPARTMENT OF AGRICULTURE

Before the

SUBCOMMITTEE ON AGRICULTURAL PRODUCTION AND STABILIZATION OF PRICES

SENATE COMMITTEE ON AGRICULTURE, NUTRITION, AND FORESTRY

MARCH 6, 1990

Good afternoon Mr. Chairman and Members of the Committee. I appreciate the opportunity to be with you today to discuss disaster protection for the American farmer.

We in the Administration, like Members of Congress, believe that it is good public policy to provide agriculture and rural economies with a safety net against catastrophic loss that meets the following criteria and objectives:

- it eases economic hardships imposed by crop failures on farmers and rural businesses, financial institutions, and rural communities;
- it reduces the financial shocks created by crop disasters;
- it enhances efficient use of farm resources; and
- it is budgetarily responsible.

Let me get right to the heart of the issue -- crop insurance has not met these criteria or the objectives set forth in the 1980 crop insurance legislation. Given current budget realities, we do not know how to fix the program so that it will be acceptable to producers and taxpayers.

Over and over again, the point has been made that crop insurance in its present form is underutilized, too expensive, and does not stop overwhelming pressure on Congress to pass annual disaster bills.

Expenditures for the combination of Federal crop insurance and ad hoc disaster assistance have averaged more than $1.1 billion annually over the period 1981-89.

The system as it presently exists just isn't working. Not from the point of view of the producer. Not from the point of view of the insurance industry. Not from the point of view of the taxpayer.

Producers have rejected the product as inadequate, complicated, and expensive. Their feelings are reflected in the market place. Less than 45% of eligible planted acres were covered by crop insurance in 1989. A portion of that coverage was due to mandatory participation for those seeking assistance under the Disaster Assistance Act of 1988. When it was voluntary, prior to 1988, participation peaked at 25 percent.

The insurance industry isn't satisfied with the program. Last July, the Commission for the Improvement of the Federal Crop Insurance Program issued a 300+ page report stating that crop insurance needs to be fixed. Their recommendations, although well intended, would add hundreds of millions to the cost of the program.

One recommendation in particular, which would allow producers to use unadjusted ASCS yields to establish coverage, would increase the total cost of the program by about 40 percent of the annual premium -- it's a nice idea, but expensive. This would have translated into an additional cost to the government of $300 million for the 1989 crop year.

The American taxpayer cannot be satisfied with the program. The program is not actuarially sound. Overall, for the period from 1980 to the present, we posted a loss ratio of 1.58. For every dollar we took in, including premium subsidy, we paid out one dollar and fifty-eight cents in claims. That is no way to run a company. FCIC spent $957 million in crop year 1988 and $954 million in 1989. In those same years we posted loss ratios of 2.4 and 1.5, respectively. The financial performance of the crop insurance program for those years is presented in an attachment to my statement.

And finally, it's apparent that many of you don't have confidence in the program. Three times in the 80's, (1986, 1988, and 1989) the Congress has seen the need to pass ad hoc disaster assistance. These actions and congressionally encouraged use of various standing disaster authorities have cost over seven billion dollars in the eighties. We have heard that a 1990 disaster bill is already being discussed.

In spite of more than two billion dollars in premium and administrative subsidies, repeated program changes, and excess losses which have added hugely to program costs -- crop insurance has still fallen short.

We need an effective, financially responsible program.

If agricultural programs in general are to remain credible with the taxpayers they must meet their goals in a budgetarily responsible manner. Ineffective programs, riddled with losses and inefficiency, must be fixed or terminated.

So what should we do?

While it may theoretically be possible to fix the program, we have been unable to figure out how to do it without adding hundreds of millions of dollars to the budget. These dollars have to come from someplace. In an era of increasingly tight funding, this is not the best allocation of scarce federal resources.

Frankly, we don't know how to substitute economic decisions for political decisions. Certain decisions, such as which crops to cover, premium rates, coverage levels, and the definition of yield are attractively political in nature. Decisions based on non-economic factors in these key areas will necessarily lead to a program which cannot be managed responsibly and will be riddled with abuse and waste. Non-economic choices also eliminate profit possibility, and preclude responsible private sector involvement.

Moreover, we don't know how to achieve sufficient participation to forestall annual disaster legislation without making crop insurance mandatory.

We know that crop insurance is not a good risk management tool for everyone. Some producers have substantial resources and can self-insure. Others engage in farming practices which diversify their risk and lessen exposure. Still others have made major financial investments such as irrigation to protect themselves from some of the risks that the multi-peril crop insurance covers.

In light of all this, we have proposed, as you know, to replace crop insurance with a standing disaster assistance program. The new program would provide payments for individual losses whenever county-wide harvested yields fall below 65 percent of normal on a crop-by-crop basis. Individual losses would be based on the difference between the producer's harvested yield and 60 percent of the normal harvested yield for the county. Payments would be based on 65 percent of the three-year average market price for that crop. There would be a $100,000 payment limitation per person. Eligibility would be limited to producers with gross annual incomes below $2 million, and compliance with certain conservation requirements would be required. Recipients would be ineligible for Farmers Home Administration disaster loans as well as the Commodity Credit Corporation emergency feed programs for the same losses.

The new program would extend to all crops currently covered under the crop insurance program, plus hay and forage. These crops account for over 93 percent of total U.S. cropland.

This disaster assistance program will continue to protect the farmer and the rural economy from the economic losses arising from widespread crop failure. In those counties where widespread losses occur, benefit levels will be similar in many respects to the 1988 and 1989 disaster bills.

The program that we propose will:

- end the need for ad hoc disaster legislation;
- be more reliable than ad hoc legislation since the producer knows that assistance will be available should the county catastrophic trigger be met;
- provide better targeting of disaster assistance to areas with catastrophic losses;
- be less costly to administer than the current crop insurance program.

The program will be triggered on county-wide losses, not individual yields. This will reduce the problems associated with encouraging production on high-risk cropping areas that occurred with the disaster payment programs of the 1970's. Producers in counties that qualify for benefits will be compensated for deficiencies in their yields from the county-wide norm.

We believe that this package will permit the private sector to develop insurance policies for producers not covered by this disaster assistance program, and we believe our proposal will provide a good environment for private sector insurance.

The trigger where Federal protection kicks in offers an umbrella for the private sector -- a ceiling on the non-independent losses against which private industry is capable of underwriting risks. Hail and fire insurance should continue to thrive. The creative forces in the private sector can offer a wide variety of policies to providers to protect them against losses which are not covered by the government. Those losses are independent in nature and appropriately borne in the private sector.

While attending the Crop Insurance Research Bureau's annual meeting a couple of weeks ago, I was heartened by the fact that several members of that organization came to me and stated their intention to work within this framework, if enacted into law, and to offer a wide variety of products.

In fact, we have already received one unsolicited letter. Perry Rutledge, President of Farmers Mutual Hail Insurance Company of Iowa, the largest writer of crop hail insurance in the nation, is ready to offer a rider for his hail insurance policy holders. He wants us to understand that he is speaking for his company only. He is enthusiastic about the opportunities to write additional coverage. I have attached a copy of his letter and supporting documents to my testimony and ask that they be entered into the record.

Whether the new policies look like the current ones, whether they protect against specific named perils or all perils, what the premiums, other terms, and the like are to be -- is open to the imagination.

That's the program. It is simple in concept. It is easy to administer. It provides a "safety net" of protection to farmers against crop failures as small as those which affect a single county. It provides benefits in eligible counties similar to the 1988 and 1989 disaster bills, thus avoiding the need to pass supplemental assistance. And, it is budgetarily responsible.

It's a departure from the experiment of the last ten years but frankly that experiment has not worked. We have been unable to come up with a better approach. We continue to be open to other ideas and will work with you to explore alternative answers.

We all agree that providing a program to assist farmers in coping with catastrophic losses is sound public policy. However, any responsible program should:

> one, provide protection for farmers and rural communities against the financial problems associated with catastrophic crop losses;
>
> two, end the need for ad hoc disaster assistance legislation;
>
> three, provide a system which permits the private sector to offer individual farmers protection; and
>
> four, achieve this with a realistic cost within the means of the current fiscal situation.

We look forward to working with you in crafting a program which will meet the needs of the producers and rural communities and fulfill the government's commitment to the taxpayers to operate an effective and budgetarily responsible program.

I will be pleased to answer any questions.

Attachment A

FEDERAL CROP INSURANCE CORPORATION
COMPARATIVE PROGRAM HIGHLIGHTS
FOR CROP YEARS 1987, 1988 AND 1989 1/
(DOLLARS IN THOUSANDS)

	CROP YEARS			
	1987 Actual	1988 Actual	1989 Estimated	Totals
Total Premium	$366,640	$436,410	$804,000	$1,607,050
Indemnities	369,161	1,053,851	1,206,000	2,629,012
Loss Ratio	1.01	2.41	1.5	1.64
Total Expenses:				
Excess Indemnities Over 1.0 Ratio	2,521	617,441	402,000	1,021,962
Direct Premium Driven Expenses:				
Premium Subsidy	87,230	109,000	201,000	397,230
Reinsurance Admin. Expenses	106,990	154,663	267,000	528,653
MMA Contract Expenses	10,388	13,618	18,178	42,184
Total	204,608	277,281	486,178	968,067
Claim Expenses Direct Policies (FCIC)	27,970	23,922	21,529	73,421
FCIC General Overhead to run Program	32,514	38,865	44,788	116,167
Total Federal Government Expenses	$267,613	$957,509	$954,495	$2,179,617

HILIGHTS:PH/2/20/90

1/ This chart represents crop year data as oppossed to financial charts which represent fiscal year data.

FARMERS MUTUAL
HAIL INSURANCE COMPANY
OF IOWA

2323 Grand Avenue
Des Moines, Iowa 50312
515-282-9104

February 9, 1990

The Honorable Clayton Yeutter
Secretary of Agriculture
United States Department of Agriculture
Washington, D. C. 20250

Dear Secretary Yeutter:

Farmers Mutual Hail Insurance Company of Iowa is, to my knowledge, the largest writer of crop hail insurance in the nation. We have never written multi-peril crop insurance for many reasons.

On February 5, 1990, you presented the Administration's proposal to eliminate FCIC/MPCI and replace this failed program with a disaster assistance program.

The question has been asked that if this happens will there be private MPCI insurance available to supplement disaster assistance. Many of the MPCI writers have said no. I say yes! Enclosed is a little paper outlining my Company's commitment to provide such a program, a rough sketch of what it would be like and an example. We are working on the details.

I am providing copies of this letter to Under Secretary Roland Vautour, Deputy Under Secretary Jonathan Kislak, and FCIC Manager John Marshall. I wish you the best of success in this matter.

Respectfully,

Perry Rutledge

Perry Rutledge
President

PR/kw
enc.

02-09-90
PERRY RUTLEDGE

A NEW KIND OF CROP INSURANCE

Since 1980, crop insurance industry people have constantly been asking me "when is Farmers Mutual Hail going to get into the multi-peril business." The answer has always been, not now. That answer is now changing.

The day after the President signs a bill eliminating FCIC and replaces it with a crop disaster assistance program similar to that proposed by Secretary Yeutter on February 5, 1990, Farmers Mutual Hail will be offering to our crop hail clients an optional named peril rider (drought and wind) at open market prices that will provide a 50% non-disappearing deductible applied to the amount of crop hail insurance carried. It will be on a farm unit basis, and each peril will be adjusted in the field by agreement with the farmer. The payment will not be affected by eligibility or indemnification for disaster assistance, and the coverage provided will be reinsured worldwide in the commercial reinsurance market.

There will be no reliance on the Federal Government for subsidy, reinsurance, or anything else and will be subject to all applicable State Insurance Department regulations, such as filing, prior approval, consumer complaint handling, guarantee funds and/or premium taxes. This will be subject to any actions at law in State courts and no Government immunity claimed.

Since 1938, the existence of the subsidized FCIC has prevented the development and marketing of this product and others like it. We can sell this to farmers who need to manage their drought risk.

02-09-90
PERRY RUTLEDGE

EXAMPLE

ASSUMPTIONS:

1. Farm is average for county
2. Three-year average market price per bushel is $1.00
3. Crop is worth: 100 bushel/acre times $1.00 per bushel = $100.00 per acre
4. No hail loss
5. Crop is total loss from a named peril. Named peril will pay: (100% loss minus 50% deductible) = 50% x $100.00 = $ 50.00
6. Disaster assistance will pay:
    - (a) County yield over 65% = -0-
    - (b) County yield less than 65% (60% loss times 65%) x $100 = $ 39.00

SUMMARY - For a total loss on a crop worth $100.00, the farmer receives:

Without disaster assistance	$ 50.00
With disaster assistance, a total of	$ 89.00

Senator Pryor. We are going to call our next panelist from the General Accounting Office, Mr. John W. Harman. Mr. Harman, we welcome you and your colleagues this afternoon, and we are very proud that you are here representing the General Accounting Office. We have a great deal of confidence and faith in your findings, and I hope we will receive your recommendations here this afternoon regarding Federal crop insurance. I am going to ask you, one, if you would mind not reading all of the statement that you have, if you can get by with it. Summarize it. We will put the full body of your statement in the record so feel free to summarize your statement at this point.

STATEMENT OF JOHN W. HARMAN, DIRECTOR, FOOD AND AGRICULTURE ISSUES, RESOURCES, COMMUNITY, AND ECONOMIC DEVELOPMENT DIVISION, U.S. GENERAL ACCOUNTING OFFICE, WASHINGTON DC; ACCOMPANIED BY CLIFF FOWLER, ASSISTANT DIRECTOR; AND JEFFREY W. ITELL, EVALUATOR-IN-CHARGE

Mr. Harman. I am prepared to do that, Mr. Chairman. We are pleased to be here today to discuss the Federal Government's responses to natural disasters affecting American agriculture during the 1980's.

Before I begin in earnest, I would like to introduce my colleagues who are at the table with me this morning. On my right is Cliff Fowler, who is Assistant Director in charge of all our work in crop production and crop assistance areas including disaster assistance. And to his right is Jeff Itell who has been doing quite a bit of work in the crop insurance area over the last several years.

Our testimony is based on the GAO report that we issued back in September of 1989,[3] and we will address first the Department of Agriculture's (USDA) role in providing agricultural disaster assistance since 1980, including the cost of providing this assistance, and secondly, criteria for assessing the Federal role in providing disaster assistance to farmers and how well current programs meet these criteria.

FEDERAL ROLE AND COSTS IN PROVIDING AGRICULTURE DISASTER ASSISTANCE BETWEEN 1980 AND 1988

Since 1980, USDA has provided disaster assistance to farmers in three different ways: cash payments, subsidized emergency loans, and an insurance program. Between fiscal years 1980 and 1988, the Federal Government has incurred costs totaling approximately $17.6 billion in support of these programs.

I will mention that the charts I will be referring to are over there to my immediate left, and they are included in the detailed prepared testimony that I have provided to the subcommittee. The first chart [4] shows the annual total costs of all these programs, and you can see that they peaked in 1981 and then again in 1988. Both of those years were drought years although there has been an upward trend ever since 1984.

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[3] Disaster Assistance: Crop Insurance Can Provide Assistance More Effectively Than Other Programs (GAO/RCED-89-211, Sept. 20, 1989).

[4] See p. 70 for Chart 1: Government Costs for Agriculture Disaster Assistance Programs (FY 1980-88).

Now the second chart [5] shows the stream of costs for each of the three programs. The broken line shows the cost for direct cash payments, totaling some $6.9 billion over that period. The thin line, the cost for crop insurance, totaling some $4.3 billion. And the thick line, the cost for disaster emergency loans, totaling $6.4 billion. The principles we used in developing criteria for determining the best way to provide disaster assistance are based largely on the premises that disaster victims should be treated equitably and consistently over time and that overall program and society costs should be minimized.

CRITERIA FOR ASSESSING CURRENT DISASTER ASSISTANCE PROGRAMS

Our criteria are derived from various GAO analyses of disaster assistance that have been conducted over the past 13 years. From this work we identified eight criteria that should be considered in devising an effective disaster strategy. These criteria are included in my prepared testimony.[6] They show that the current crop insurance program satisfies more criteria than the other two programs. Specifically, the crop insurance program satisfied three of the eight criteria. The direct disaster assistance payment program satisfied one while the loan program did not satisfy any.

And with further improvements to the crop insurance program, it could satisfy even more criteria. In reaching this conclusion, that is that the crop insurance program satisfies more of the criteria, we recognize that that program has had a history of management and delivery problems that in the short term makes it difficult to justify the current programs of sole source of disaster assistance to farmers. We certainly have been one of the chief critics of that program in terms of its management.

Consequently, if the Congress chooses to rely on the crop insurance program exclusively to provide crop insurance assistance or crop disaster assistance, a transition period for strengthening the program would be necessary. Also, a viable crop insurance program as envisioned by the Congress, and this is, we think, a very important point—a viable program as envisioned by the Congress in 1980 will in all likelihood not be realized as long as it has to compete with direct assistance and loan programs. These programs have received larger amounts of Federal funds and have had more attractive terms for farmers.

Consequently, the crop insurance program's participation rates have remained low, and the program has never developed an actuarially sound program. We believe a restructuring of the agriculture disaster programs that removes this disadvantage could help determine how effective the crop insurance program can be. As you know, Mr. Chairman, the administration as you discussed in its 1990 farm bill proposal has recommended replacing the crop insurance program with legislated disaster assistance program similar to the 1988 and 1989 ad hoc programs. Because the administration's proposal is patterned after these disaster programs, we believe that crop insurance would be a more equitable and efficient way to provide disaster assistance.

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[5] See p. 71 for Chart 2: Government Costs for Direct Payment, Emergency Loan, and Crop Insurance Programs (FY 1980–88).

[6] See p. 72, Appendix I: Chart showing how well different forms of disaster assistance meet the criteria.

That completes my summary. We would be pleased to answer any questions that you may have.

Senator PRYOR. Mr. Harman, Senator Kerrey and Senator Bond and I, as all the members of this committee do, we represent farmers. We are trying to determine what is best for the farmer. What is best for the farmer today? What course should we pursue?

Mr. HARMAN. We believe for a variety of reasons, which were laid out in that report, and using those eight criteria, which we think can be used to judge any particular proposal, that crop insurance, a properly structured crop insurance program, is the best program for farmers. It is a more equitable program. It gets away from the kind of problems you have with the proposal that the Department of Agriculture has given in terms of having county controlled disasters as opposed to individual disasters where an individual would have a disaster and he is not able to get any benefits because that county was not declared as a disaster area.

Senator PRYOR. You think this is one of the shortfalls, then, of the administration's proposal?

Mr. HARMAN. Yes, it is, although I would agree with much of what they said in terms that something has to be done. The crop insurance program is not working today like it should. There are a lot of complaints. We have run into those complaints when we talk to farmers. Some of the complaints you all have mentioned in discussions with agriculture and USDA representative. So we do need improvements. We have needed management programs. We need improvements in the delivery of crop insurance. We do not feel that crop insurance really has been given a fair chance because it has had to compete with these other programs, and because of these weaknesses in the program.

Senator PRYOR. All right. On that point, Mr. Harman, you are regarded as a true professional. You have had many years, I understand, with the General Accounting Office.

Mr. HARMAN. Yes, sir, I have.

Senator PRYOR. And you also have been interested in this issue, I think, for some time; is this correct?

Mr. HARMAN. Well, the General Accounting Office has been in this issue for some 13 years. I have been in it probably for about 5 or going on 6 years now.

Senator PRYOR. Now when you do a study and a workup like this, I assume that you have to have an awful lot of contact and support from the USDA about the Federal crop insurance program? This is a question that requires a subjective answer. Did you find enthusiasm at USDA for the Federal crop insurance program?

Mr. HARMAN. Well, over the period of time, and I might let my colleagues respond to that question also since they have dealt with them over this period.

Senator PRYOR. Colleagues, what kind of enthusiasm at USDA did you find for the Federal crop insurance program?

Mr. HARMAN. Notice how I managed to pass that question on very——

Mr. Fowler. Mr. Chairman, I have been sort of——

Senator Pryor. You dodged that one well, Mr. Harman. And I understand. Excuse me. Go ahead, sir.

Mr. Fowler. I guess I have been sort of the point man for GAO in crop insurance for the last 5 or 6 years, and I have dealt with the staff there extensively. I think an honest answer would be in the last year or two I have seen a greater enthusiasm. I have seen better management. I think what I have seen over the years in that program that has hurt the program has been bad management up until the last year or so or two. I think things are moving in the right direction from a management standpoint. I have observed that.

Senator Pryor. All right. Thank you, sir. Any follow on to that?

Mr. Itell. I agree.

Senator Pryor. Thank you. Mr. Harman, I am going to now let Senator Kerrey, I will turn the questions over to Senator Kerrey.

Senator Kerrey. Just a followup on that point. I guess I should observe for the record that when it comes to insurance, I think an awful lot of us do not like it until we need it. I can recall purchasing property and casualty insurance when I first went into business and I thought it was a waste of money. If you had asked me to provide some opinion about property and casualty insurance in 1972, 1973, and 1974, I would have said I spent $12,000 a year and I got nothing. If you would have asked me in 1975 after a tornado blew my business away, I would tell you it was the best investment I ever made.

One of the difficulties that I have with crop insurance, particularly given the way that it has been managed, is that it has not been given a fair test. It is hard to get an analysis that gives me a great sense of what we need to do to, in fact, improve it. I know we have some recommendations that were made and I am just curious. I am not that familiar with the charges you were given to prepare this report, but did you do any sort of qualitative analysis about what could be done to make this program work better? You mentioned management and delivery of product. Do you have any specific recommendations that you can make for us?

Mr. Harman. Well, there are several things we have said in our issued reports to deal with the issue of loss adjustment. That is one area that gave us a great deal of problems, the large number of losses that were being paid out by FCIC. And I think Senator Bond sort of alluded to that problem in terms of what he experienced in Missouri. But for that management problem and how you get ahold of and get control over the loss situation, we have made several recommendations.

Also, we did some work on why the participation rates were so low, and we had several recommendations in that area in terms of going out and making this into more of a market-oriented organization that can determine what our customer wants and what does our customer need and what are we supplying, and do our needs—and we cannot supply an insurance program that is going to apply across the country to everyone equally in terms of what everyone needs because the needs are different in Missouri than they are in Nebraska or other locations.

So we have to have that ability. And I have to admit that we have spent 13 years over the period of time—ourselves here, probably 5 or 6 among us—and we do have thoughts about—although the Office has not taken any particular position on what we think a good option would be, nor have we evaluated any particular options. We have looked into this to some extent over the past several months. We have looked at the Commission's report, and believe that crop insurance can be changed. I think probably the one option that has been raised to us, and we had done some thinking about, although we have done no detailed analysis, is the one that Senator Bond referred to, which would have some sort of insurance up to a certain point, insurance that can be rated, insurance that is true insurance, and that the companies can feel comfortable in providing. And then add some sort of catastrophic rider on to that that may even be free, as a way of encouraging people to take that insurance.

And it seems to us that that would make these programs complement each other rather than compete with each other, and also, of course, have another tier that would provide some risk for the producer in the sense of some sort of deductible that they would have to satisfy.

Senator KERREY [presiding]. Senator Bond, you may be happy to know that before you came, I asked Mr. Kislak a question about how he scores their proposal and because it is a contingent liability, he says OMB scores it as zero. So I assume he will score your proposal at zero as well. So you can know that you have in your hands a proposal that will not cost us anything. Do you have any questions?

Senator BOND. I think leaving that comment aside, Senator Kerrey, we may have a chance to discuss that later, but Mr. Harman, I understand you all are not making any specific recommendations on how it can be made to work better, how we can get rid of the abuses in the program?

Mr. HARMAN. Well, we have made recommendations in the past on abuses, particularly in loss adjustments. And we have even gone so far as to try to determine if there is an incentive in the reinsured agreement that would provide some sort of reason why these losses are occurring. We had a 30 percent, I think, rate, error rate, back in—I think it was——

Mr. FOWLER. 1987.

Mr. HARMAN [continuing]. 1987. We looked at it. That dropped to 16 percent when we looked at the 1988 figures. But the question on a 16 percent error rate on loss adjustment, is that acceptable? We would probably say no. But there has been improvement, and as Cliff said, there has been major improvement in the management. And they have increased the oversight over reinsured companies. They have taken action against some reinsured companies that have not acted in good faith. So we have made a number of recommendations aimed at management.

Senator BOND. One of the most interesting management recommendations you make in here at the bottom of page 2[7] of your written statement, you say, "Consequently, if the Congress chooses to rely on crop insurance as the primary method of providing disaster assistance, it should prevent other disaster assistance programs from competing with it," that is, being enacted by Congress. Now there are some who may suggest that it would be safer to transport lettuce by rabbits than to assume that Congress would not respond to a disaster. Do you have a means of suggesting how that would be accomplished?

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[7] See p. 58 for John W. Harman's prepared remarks.

Mr. **Harman**. That is a good point. I think it would have to be through some method like the one I just mentioned. It has to be where the only way that producers can get protection against disasters is through a crop insurance program.

Senator **Bond**. And we would prevent ourselves from—you let me know when you get 51 Senators to sign on to commit never to support disaster relief, would you?

Mr. **Harman**. That is a very difficult problem, but our viewpoint is unless you can do that——

Senator **Bond**. Has Canada been able to do it?

Mr. **Harman**. Canada, as far as I know, has not been able to do that.

Senator **Bond**. And they have rates up 70 to 80 percent on, do they not?

Mr. **Harman**. But I think also if you look at the proposal, the type of—and we are not pushing this particular proposal—if you look at that, if you had that catastrophic rider that Congress would have to appropriate funds for through some sort of funding mechanism and have FCIC or a similar organization that would provide regulatory, have regulatory authority over the whole process, that is one option, at least to us, it looks like one we may want to look at. But if you cannot—and I said this on the House side in testifying on this subject—unless there is political willpower to avoid doing that to any great extent—and there are always going to be some crops, I think, we are going to have to do that with. There are some crops that we are just not going to be able to cover through insurance. But unless we do that, then——

Senator **Bond**. Essentially that is the best mechanism that we have been able to come up with is a permanent catastrophic disaster program. Maybe it is not foolproof, but it seems to be the best idea. Let me turn to the criteria, the eight criteria you have in this booklet,[8] and frankly, it seems to me that these are somewhat subjective on how you go down. A number of the areas you put "depends" and you suggest some of the qualifications that perhaps we ought to be taking a look at.

But the amount of—Criterion No. 1—The Amount of Disaster Assistance Provided Should Be Determined by the Amount of a Farmer's Loss, Not by the Severity of the Disaster. You say crop insurance meets it; disaster payments do not. Would the disaster payment meet that criteria if it did not require a county-wide disaster declaration?

Mr. **Fowler**. It could. My answer to that would be it could. And the reason I say that is it would depend on the coverage, the catastrophic portion; to the extent farmers were covered for a catastrophic incident, it would. But up to that point, it would remain a question mark to me on the extent to which they would be covered if they would choose to buy crop insurance.

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[8] See Appendix II, Comparison of Disaster Assistance Programs, Criteria for Weighing the Merits of Current Forms of Disaster Assistance, GAO/RCED-89-211, pp. 24-35.

Senator BOND. Well, crop insurance, you are going to say that you are going to try to provide crop insurance for a 5 or 10 percent loss?

Mr. ITELL. The distinction here is that crop insurance is available before the crop-year. A farmer does not know under the current program, in the ad hoc programs, when there is going to be a disaster program. Under the administration's proposal where you have a standing disaster assistance program, direct payments would meet that criterion.

Senator BOND. Well, down here on Criterion No. 7, Disaster Assistance Program Should Have Predictable Annual Costs. That is a heck of a good guess there. You say it depends. Well, frankly in both of these, I think that about the only way you could do it, you give the crop insurance the benefit of a "depends"—disaster payment benefit or no benefit, just say no. But if you had a crop insurance, private crop insurance system, which set out in advance a set subsidy for the premiums, then you could construct a program that would have a predictable annual cost.

Mr. ITELL. If they are not sharing in the losses with the insurance companies.

Senator BOND. Yes, and that is——

Mr. ITELL. It is good to know.

Senator BOND. That is one of the problems.

Mr. ITELL. Yes.

Senator BOND. And I think you put the incentives in the wrong place when you open up the Treasury short of a disaster, a catastrophic disaster, to that payment. Let us see. It says, you have here Criterion 5: Disaster Assistance Programs Should Be Consistently Available Over Time to Allow for Long-range Planning. Again, that could be addressed by the alternatives that we have discussed. Did we ask about Criterion No. 2, Disaster Assistance Programs Should Provide Similar Amounts of Assistance to Farmers Suffering Similar Amounts of Losses? Why do you score both crop insurance and disaster payments no? What could you do to satisfy that criterion?

Mr. HARMAN. Well, it is very difficult to satisfy that criterion largely because it is impacted by the Tax Code, and that is what we are getting at there. The Tax Code and the way the Tax Code works, of course, people in the higher brackets of the Tax Code have more benefits as a result of disaster than do others. For instance, in the loan program, it definitely does not satisfy that criterion because under a loan program they can take that loss because theoretically they are going to pay the loan back. Also, in the disaster programs, it does have, the Tax Code has different impacts on, differing impacts on what these people receive in total benefits.

Senator BOND. I guess if you carry it out that far, you are going to have a tough time getting any of these——

Mr. HARMAN. Yes, it is very difficult. It is almost——

Senator BOND. I mean this is an unmeetable criterion then. So we should not worry about that.

Mr. HARMAN. Right.

Mr. FOWLER. Yes.

Senator BOND. Well, I think those are the main questions I have. I will not take up further time.

Mr. HARMAN. Senator, we are very pleased to see that you are using our reports so thoroughly.

Senator BOND. Well, it is good to make notes on and—— [Laughter.]

Senator BOND [continuing]. I certainly have found it, let us say, interesting to read your views on that. Thank you, Mr. Chairman.

Senator KERREY. Senator Harkin.

Senator HARKIN. Thank you very much, Mr. Chairman. I too want to thank you for your report. Looking at this, again, when you look at the chart of the amount of government cost 1980 to 1988, you see an interesting thing. Federal crop insurance started in 1981. That was the all crop/all risk insurance program that passed and 1981 being the first year it was implemented. The cost started going down. It went down in 1982. It went down in 1983 and it went down in 1984. It only started going up appreciably after 1985. It went up a little bit, it looks like, in 1985. Then you hit 1986, 1987, and 1988 when the drought years were happening.

Light drought year in 1986, big drought in 1987, big drought in 1988. So when you look at that, you are looking at a small slice of time and judging the entire program by that small slice of time. Now I am not saying you are. But I am saying that the proposal that we are getting from the administration. You know you average that out and you look at what has happened there during those years, it is not all that bad a deal. Now I said before, and I remember when this whole thing came through in 1980, we left the provision in there that the disaster program was left in as a back up provision in the 1980 bill.

So we never really had a true test of crop insurance as to whether or not people would take it or not without some kind of other safety net. Secondly, we never—at least I think I got this out of your report, too—we never really had a determined marketing effort on Federal crop insurance, a determined educational program by the Federal Government to go out and educate farmers about Federal crop insurance. And thirdly, we never had an effort by the Federal Government to really increase the risk pool, to really go out and really increase the risk pool, and to even out the disparities in crop insurance from county to county.

I have counties in Iowa, one county where the coverage is $8, $9 per acre difference from one county to the next just on corn. Again, it is a classic example, as I have said before, where if you ask a farmer why they do not take crop insurance, the answer is basically the costs are too high and the coverage is too low. We ask the Federal Crop Insurance Corporation why more farmers, or why their prices are so high and their coverages so low, and they say because more farmers do not take it. Something has to break this. If you could widen that pool, if you could get 80, 90 percent participation, you would have that risk pool. And as any insurance person can tell you, the bigger the risk pool, the better your coverage, the lower the rates. But we have never been able to get there.

Do you have any thoughts or any ideas on how we could increase that risk pool without making it mandatory? You know go out and increase that risk pool to get it up to that 80 to 90 percent level?

Mr. HARMAN. One thing you have to do is make it an attractive product like any product that you are trying to sell. It has to be an attractive product, and it seems to us in some of the work that we have done that it is not always an attractive product for the farmers and some of that has to do with cost. Some of it has to do with paperwork. There are any number of reasons. I think another thing that has to be done is take it out of competition with disaster assistance payments, primarily disaster assistance payments. In other words, a farmer should not have that choice. If he wants to be covered for disaster assistance, the insurance route is the way to go.

Now I am not saying that insurance is the only way. That, as we said earlier, it could be backed up by some catastrophic provisions which are basically the disaster payment programs, but working through the insurance program. I do not know. Cliff, you might talk a little bit about some of the work we did on that.

Mr. FOWLER. Well, if I could add one thing to that. I think one of the things that has really hurt, and it is coming out in the discussion today, is in the past FCIC has tried to insure against the large catastrophic incidents. I am not really sure from what I learned you could do that. I think you have to break it out and have a free rider for catastrophic protection for those that buy crop insurance, for example, or some scenario like that to make it a better product, to make FCIC look better, to get it on a better financial footing.

I mean it has taken a lot of hits for that and justifiably so. But to permit them to stop necessarily insuring against the big hit that we have experienced 2 years recently, I think would really help. And I think you are going to have to break that out somehow and let them insure against what they can insure against because you cannot insure against catastrophic losses. I am told, from actuaries and other people, that you need such a long time span to get a basis for those, that it is essentially uninsurable.

Senator KERREY. You guys in a hurry?

Mr. HARMAN. We are at your discretion, Mr. Chairman.

Senator KERREY. Oh, you never want to say that.

Mr. HARMAN. We at GAO always operate under that.

Senator KERREY. Would you mind? Senator Harkin, one of the things that I would personally find useful would be to ask the next panel to come up and have you guys stay around for when we ask questions.

Mr. HARMAN. Fine.

Senator KERREY. We might be able to get some sort of discussion going because the next panel is composed of the people that made up the Commission that made the recommendations that we received last year.

Mr. HARMAN. Fine.

Senator BOND. Mr. Chairman, I might just make one comment as a followup. You are talking about the need for the catastrophic coverage. Frankly, one of the reasons why this seems on its face to make some sense is that when you have a catastrophic event, under, at least under our current system of target prices and deficiency payments, we have been able to cover the cost of the catastrophic or the disaster payments by a reduction in deficiency payments. At some day in the future if we do not have target prices, and maybe you have a different situation, but under our current system, the catastrophic disaster usually is accompanied by a reduction in supply which increases the price which limits the deficiency payment. And that is, I think that is the basis on which you get some equilibrium on the catastrophic end of it. Thank you, sir.

Senator PRYOR [presiding]. Where are we now in questioning? Which Senator?

Senator HARKIN. He just dismissed this panel and asked them to stand by. Senator Boschwitz has arrived. Senator Boschwitz, these gentlemen are from the General Accounting Office. Would you have any questions?

Senator BOSCHWITZ. I am sorry. As you know, we came in together, Mr. Chairman, and I have not reviewed their testimony. But, and I know that they have been critics of the crop insurance program. I presume that in your testimony you have described to the subcommittee how you think that the crop insurance program can be made viable and whether or not you feel it can be made viable?

Mr. HARMAN. Yes, we do, Senator Boschwitz. The testimony we have presented today really used criteria we developed to measure the different types of disaster assistance programs that have existed over the last 10 years or so, and measured against that criteria we felt crop insurance is the way to go. But that we think changes have to be made to that program, have to be made to that program in terms of some management changes that are already underway, changes in marketing the product, changes in perhaps how the whole system is structured to make sure, to increase participation in the crop insurance.

Senator BOSCHWITZ. And so you think it is a system that can be used without having the disaster program?

Mr. HARMAN. It depends on how you structure it. And it can be done, but it has to be done in a way that the whole system operates through an insurance program with perhaps a catastrophic, as we discussed here a few minutes ago, a catastrophic rider that would allow for taking care of these catastrophic events such as the 1988 drought.

Senator BOSCHWITZ. That was an extraordinary one as that chart would indicate. And did you find in your examination of crop insurance that some people abused the system, planted only for the crop insurance?

Mr. HARMAN. Well, I would not—it is very difficult from a GAO——

Mr. ITELL. We found a large—well, you can talk about it.

Mr. HARMAN. Go right ahead.

Mr. ITELL. The loss adjustment report. We have done two studies on loss adjustment. We found that there are a lot of errors that can be caused by a lot of different reasons, but that there were a significant amount of overpayments in 1987. In 1989 when we conducted a followup study, it seemed like there was less overpayment.

Senator BOSCHWITZ. I understand that part of the criticism of crop insurance has been concerning the quality of the adjusters. That the adjusters were not experienced people. I am not sure that experienced people can be reasonably found on the other hand. It is seasonal work to adjust crop losses. Did you find that one of the problems was also in the adjustments?

Mr. ITELL. Right.

Senator BOSCHWITZ. They were spotty.

Mr. HARMAN. We did find instances where we thought it was serious enough to refer to the Inspector General, particularly the 1987 report, yes.

Senator BOSCHWITZ. Did you find any instances of farmers who had the rather marginal land who would plant for the crop insurance? I know that some of my farmers think that that happens.

Mr. HARMAN. That was always something that was raised and I think you are probably referring to a process that we refer to as adverse selection where the county-wide average was used for yields, and as a result it encouraged planting by farmers who had marginal land because they could never reach the yields, achieve the yields of the county; therefore they would always be paid. Whereas, the better farmers that you need to spread your risk would not participate because they would not be paid.

Senator BOSCHWITZ. You found instances of that?

Mr. HARMAN. There were instances of that.

Senator BOSCHWITZ. Well, it would be my hope, Mr. Chairman, that we look at the crop insurance program in some greater detail. From my standpoint, if we had a choice, we would have a good crop insurance program that would not require disaster assistance. That may not be practical or practicable, but I know that the crop insurance program does not insure some crops. It does not insure among other crops, the yields properly or adequately, and there is much criticism of it. And it would be my hope that in this bill we are able to make crop insurance a viable and useful tool once again. I apologize for being late, Mr. Chairman.

Senator PRYOR. We are proud you are here, Senator Boschwitz, and thank you for your questions. Mr. Harman, I am going to call the next panel. However, I am going to ask if you would be so kind as to remain where you are. We will put our panel 4 across the table because it might be good to have an interchange between all of us here.

[The prepared statement and attachments of Mr. Harman follow:]

United States General Accounting Office

GAO

Testimony

For Release
Expected at
2 p.m. EST
March 6, 1990

Roles, Cost, and Criteria for Assessing Agriculture Disaster Assistance Programs Between 1980 and 1988

Statement of
John W. Harman, Director, Food and
Agriculture Issues
Resources, Community, and Economic
Development Division

Before the
Subcommittee on Agricultural Production
and Stabilization of Prices
Senate Committee on
Agriculture, Nutrition and Forestry
United States Senate

Mr. Chairman and Members of the Subcommittee:

We are pleased to be here today to discuss the federal government's responses to natural disasters affecting American agriculture during the 1980s. Our testimony will address (1) the Department of Agriculture's (USDA) role in providing agricultural disaster assistance since 1980, including the cost of providing this assistance, and (2) criteria for assessing the federal role in providing disaster assistance to farmers and how well current programs meet these criteria. My statement today is primarily based on a GAO report issued in September 1989.[1]

In summary, USDA has provided disaster assistance to farmers through direct cash payments, subsidized emergency loans, and a crop insurance program. Between fiscal years 1980 and 1988, the federal government has incurred costs of approximately $17.6 billion in support of these programs: $6.9 billion for direct cash payments, $6.4 billion for disaster emergency loans, and $4.3 billion for crop insurance.

In developing criteria for determining the best way to provide disaster assistance, we relied on two basic principles--equity and efficiency. Under an equitable program, disaster victims should be treated consistently over time. With an efficient program, costs should be minimized. On this basis, we identified eight criteria that should be considered in devising an effective disaster assistance program.

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[1] Disaster Assistance: Crop Insurance Can Provide Assistance More Effectively Than Other Programs (GAO/RCED-89-211, Sept. 20, 1989).

Application of our criteria to the three existing programs shows that crop insurance satisfies more criteria than the direct payments or emergency loan programs. Specifically, we found that crop insurance would satisfy 3 of the criteria, while direct payments would satisfy 1, and emergency loans none. We also found that if some program characteristics were changed, crop insurance could satisfy 7 of our criteria, and the direct payments and emergency loan programs 4.

In concluding that crop insurance is a better way of providing disaster assistance than either the direct payment or emergency loan programs, we believe that the real effectiveness of the program cannot be fully determined as long as it has the disadvantage of competing with the other disaster assistance programs. Consequently, if the Congress chooses to rely on crop insurance as the primary method of providing disaster assistance, it should prevent other disaster assistance programs from competing with it.

FEDERAL ROLE AND COSTS IN PROVIDING AGRICULTURE DISASTER ASSISTANCE BETWEEN 1980 AND 1988

Let me now briefly discuss the federal role and costs in providing agriculture disaster assistance since 1980.

Throughout the 1980s, USDA has been responsible for administering three types of disaster assistance programs--direct cash payments, subsidized loans, and subsidized insurance. Each of these programs helps farmers deal with a loss of income if their crops are damaged or destroyed by natural causes.

Before 1980, USDA provided disaster assistance mainly through direct cash payments and loans. New legislation was enacted in 1980 that greatly expanded the scope and availability of crop insurance.[2] At the time, the Congress believed that an expanded crop insurance program covering more crops and a larger part of the country would alleviate the need for expensive, ad hoc disaster assistance programs.

Despite the expanded scope and availability of crop insurance, the Congress has continued to provide disaster assistance to farmers through direct payment and emergency loan programs during the 1980s because crop insurance participation rates have remained relatively low.[3] Low participation rates, in turn, have encouraged the Congress to establish ad hoc disaster assistance programs, which further undermined crop insurance participation. This cycle of initially low participation rates leading to competing programs, which further discouraged farmers from purchasing crop insurance, limited the program's effectiveness and led us to today's dilemma of providing competing disaster assistance programs.

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[2] The Federal Crop Insurance Act of 1980 (P.L. 96-365, Sept. 26, 1980).

From 1980 through 1988, USDA spent approximately $17.6 billion to support the direct payment, emergency loan, and crop insurance programs. As indicated in chart 1, total costs for all three programs have increased every year since 1984. Chart 2 shows the costs for each of the three programs for fiscal years 1980 through 1988.

Direct payments have cost a total of $6.9 billion, reaching peaks of $1.4 billion in 1981 and $4 billion in 1988 as a result of especially severe droughts in those years. The costs of the Disaster Assistance Act of 1988,[4] which include 1989 outlays, are included in chart 2 under costs for fiscal year 1988.

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[3] Since 1980, the amount of eligible acres enrolled in the program has risen from 9.6 percent in 1980 to 24.5 percent in 1988, well below the 50-percent target established for the program in 1980. In response to the severity of the 1988 drought and crop insurance purchase requirements, participation rates rose to about 40 percent in 1989.

[4] P.L. 100-387, Aug. 11, 1988.

USDA's emergency loan program costs were $6.4 billion from 1980 through 1988 and have been increasing steadily throughout the decade. Specifically, emergency loan program costs have risen from $245 million in 1980 to over $1.6 billion in 1988. Although most of the total costs have been due to interest subsidies, an increasing part of the rise in costs has been due to rapidly increasing loan defaults leading to debt write-offs.

The federal share of crop insurance costs since 1980 is about $4.3 billion. As was the case for other forms of disaster assistance, the federal costs for supporting crop insurance also increased during the decade. Total government contributions for the crop insurance program increased from $28 million in 1980 to $1.2 billion in 1988.

CRITERIA FOR ASSESSING CURRENT DISASTER ASSISTANCE PROGRAMS

Now, I shall briefly discuss our criteria for assessing federal disaster assistance programs to farmers and how well current programs meet these criteria.

In developing these criteria, we have taken the position that the policy principles of equity and efficiency are essential elements of any desirable disaster assistance program. These principles suggest that an equitable disaster assistance policy ensures that aid is provided consistently to victims suffering from similar losses over time. An efficient disaster assistance policy ensures that benefits are provided at the lowest possible cost to government and to society as a whole. In our opinion, an equitable and efficient disaster assistance policy should

(1) determine compensation by the amount of a farmer's loss, not by the severity of the disaster,

(2) provide similar amounts of assistance to farmers suffering similar amounts of losses,

(3) not provide farmers more assistance than the amount of their disaster losses,

(4) not create incentives to encourage farming practices that increase the likelihood and extent of losses,

(5) make the programs consistently available over time to allow for long-range planning,

(6) help farmers withstand and recover from the effects of natural disasters,

(7) provide predictable annual costs, and

(8) meet their objectives at the lowest possible cost.

Our analysis of how well each of the current programs satisfies these 8 criteria shows that the crop insurance program satisfies 3, the disaster payments program satisfies 1, and the emergency loan program satisfies none. (See app. I.) If some program characteristics were changed, these programs could satisfy 7, 4, and 4 criteria, respectively.

Our first criterion is that the amount of disaster assistance provided should be determined by the amount of a farmer's loss, not by the severity of the disaster. Crop insurance meets this criterion. The direct payment and emergency loan programs do not. Ad hoc approaches to disaster assistance policy, in which disaster relief programs or program terms are established after the major disaster has occurred, can result in different treatment for similarly affected disaster victims. In contrast, the terms of compensation under crop insurance are determined before a disaster occurs and, therefore, crop insurance provides farmers equitable assistance more consistently.

Our second criterion is that disaster assistance programs should provide similar amounts of assistance to farmers suffering from similar amounts of loss. None of the programs meet this criterion. All three programs provide some disaster benefits indirectly through the tax code, primarily as deductions to income. Because the value of these deductions is higher for taxpayers in higher tax brackets than for taxpayers in lower tax brackets, similarly affected disaster victims may obtain different levels of total assistance from a given program if they are in different tax brackets. Because emergency loan recipients can deduct their entire disaster loss, and direct payment and insurance recipients cannot, tax benefits under the emergency loan program may be more substantial than under the other two programs.

Our third criterion is that disaster assistance programs should not provide farmers more assistance than the amount of their disaster losses. None of the programs meet this criterion, but they could with program changes.[5] Farmers in all three programs may receive disaster assistance on the basis of county average production data, which can be higher than their actual production histories. Therefore, under some circumstances, farmers can be compensated for more than their losses under all three programs.

Criterion four is that disaster assistance programs should not create incentives to encourage farming practices that increase the likelihood and extent of losses. None of these programs meet this criterion, but they could come closer to meeting the criterion with program changes. Subsidized disaster assistance programs discourage farmers from taking risk-reducing measures because, with subsidies, farmers may be able to obtain disaster assistance that provides nearly complete protection at a cost lower than prevention. Generally, the more a program is subsidized, the less likely it is that farmers will try to reduce risks. To the extent that all three programs are subsidized, they do not meet this criterion.

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[5] In the following discussion, program changes needed for programs to meet criteria are identified as footnotes in appendix I.

Criterion five is that disaster assistance programs should be consistently available over time to allow for long-range planning. Crop insurance meets this criterion. The direct payment and emergency loan programs do not. As other business managers, farmers must make decisions about risk and the extent of protection their enterprise requires from events beyond their control. For example, the availability of direct payment and emergency loan programs has varied significantly over time, making it difficult for farmers to develop risk management plans. In contrast, crop insurance has provided disaster assistance more reliably. Once a crop insurance program has been established in a county, it has remained available for farmers in that county year after year.

Criterion six is that disaster assistance programs should help farmers withstand and recover from the effects of natural disasters. Crop insurance and the disaster payment program meet this criterion. The emergency loan program does not meet this criterion, but it could with program changes. Simply put, disaster assistance experience in the 1980s indicates that cash assistance, in the form of direct payments or insurance indemnity payments, helps farmers recover better from natural disasters than assistance in the form of loans. Loan programs do not provide farmers any of their expected income (unless the loan is forgiven) and increase farmers' debt burdens, which makes it difficult for some farmers to obtain financing for normal operations and to recover from future disasters.

Criterion seven is that disaster assistance programs should have predictable annual costs. Crop insurance does not meet this criterion, but it could with program changes. The direct payment and emergency loan programs cannot meet this criterion. Costs could be made more predictable if the programs were managed in a way in which program costs are determined in anticipation of catastrophic events. Neither the direct assistance nor emergency loan programs have predictable costs. And although crop insurance was established to operate this way, it also does not have predictable costs because in only about one-half of the current program do policy premiums reflect the true risk of written policies.

Our last criterion is that disaster assistance programs should meet their objectives at the lowest possible cost. None of the three programs meet this criterion, but they could with program changes. As noted earlier, disaster assistance programs can meet their objectives at lower costs by incorporating incentives to reduce risky farm practices. However, subsidized disaster assistance programs discourage farmers from taking risk-reducing measures. Therefore, none of the three programs fully meet this criterion because all are subsidized.

In addition, offering farmers more than one form of disaster assistance, as in 1986 and 1988, increases the probability that USDA would spend more for disaster assistance than if only one form of assistance were available to a farmer. For example, more could be spent when ad hoc direct payment programs provide crop insurance policy holders additional benefits so they are not penalized for purchasing insurance.

OBSERVATIONS

In concluding that crop insurance meets more of these criteria than other forms of assistance, we recognize that the crop insurance program has had a history of management problems that, in the short term, makes it difficult to justify the current crop insurance program as the sole source of disaster assistance to farmers. Consequently, if the Congress chooses to rely on the crop insurance program exclusively to provide crop disaster assistance, a transition period for strengthening the program probably would be necessary.

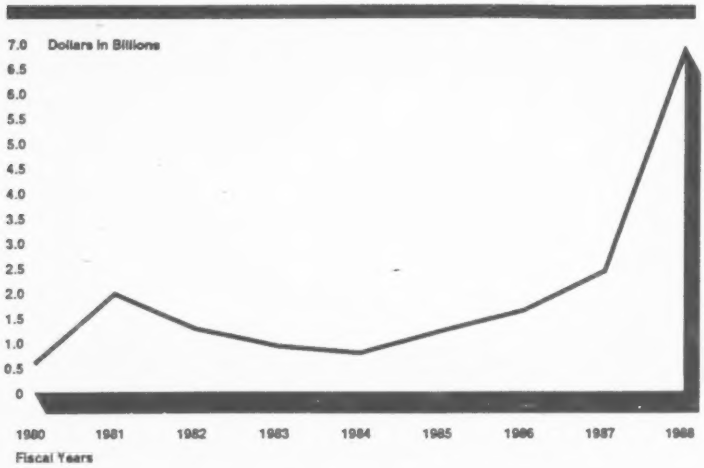
Another critical problem that the crop insurance program faces is that it has had to compete throughout the 1980s with direct assistance and loan programs, which have received larger amounts of federal funds and have had more attractive terms for farmers. Consequently, its participation rates have remained low, and it has never developed an actuarially sound program. We believe a restructuring of the agriculture disaster assistance programs that removes this disadvantage could help determine how effective the crop insurance system can be.

We also recognize that crop insurance is only appropriate for compensating victims who lost crops owing to a disaster. Other forms of assistance, including alternative insurance programs, would be more suitable for disaster-caused damages to farming and ranching infrastructure, such as the destruction of a barn, to help restore the productive capacity of a producer's enterprise.

As you know, Mr. Chairman, the Administration, in its 1990 Farm Bill proposals, recommends replacing the crop insurance program with a legislated disaster assistance program similar to the 1988 and 1989 disaster payment programs. The new program would provide direct payments for individual losses whenever county-wide harvested yields fell below 65 percent of normal yields on a crop-by-crop basis. We have not studied the Administration's proposal in detail. However, because the Administration's proposal is similar to previous disaster payment programs, we believe crop insurance, as we stated earlier, would be a more equitable and efficient way to provide disaster assistance.

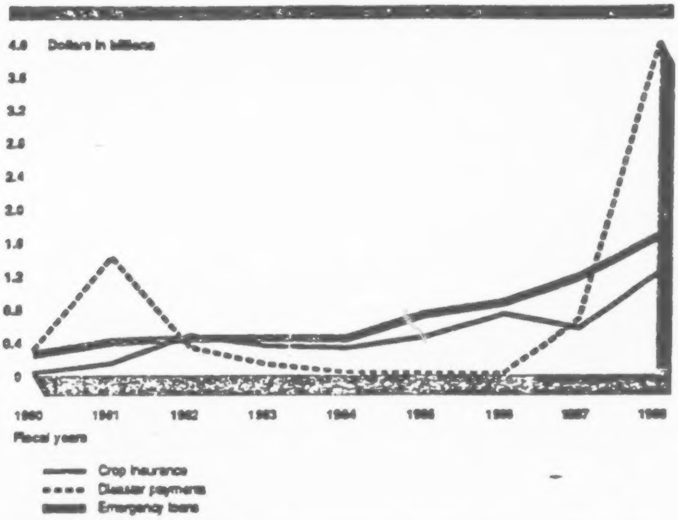
Mr. Chairman, this concludes my prepared statement. My colleagues and I will be happy to answer any questions you may have.

Chart 1: Government Costs for Agriculture Disaster-Assistance Programs (FY 1980-88)



Note: Chart represents actual government costs not adjusted for inflation
Source: USDA

Chart 2: Government Costs for Direct Payment, Emergency Loan, and Crop Insurance Programs (FY 1980-88)



Totals for FY 1988 include disaster assistance payments made in FY 1989. Administrative costs for FY 1980 are not included.

Total emergency loan administrative costs for FY 1980-81 are not included. Administrative costs for those years only include money received from the revolving fund.

Source: USDA.

CHART SHOWING HOW WELL DIFFERENT FORMS OF DISASTER ASSISTANCE MEET THE CRITERIA

Criteria	Crop Insurance	Disaster Payments	Emergency Loans
1. The amount of disaster assistance provided should be determined by the amount of a farmer's loss, not by the severity of the disaster.	Yes	No	No
2. Disaster assistance programs should provide similar amounts of assistance to farmers suffering similar amounts of losses.	No	No	No
3. Disaster assistance programs should not provide farmers more assistance than the amount of their disaster losses.	Depends[a]	Depends[a]	Depends[a]
4. Disaster assistance programs should not create incentives to encourage farming practices that increase the likelihood and extent of losses.	Depends[b]	Depends[c]	Depends[b]

[a] Would meet criterion if actual production histories were used exclusively.

[b] Would meet criterion to the extent that programs were not subsidized. For crop insurance, incentives would be reduced to the extent that premiums reflected actual risks and that subsidization of high-risk participants by low-risk participants was minimized.

[c] Would meet criterion to the extent that losses are only partially compensated and that compensation for risky farming practices was prohibited.

	Criteria	Crop Insurance	Disaster Payments	Emergency Loans
5.	Disaster assistance programs should be consistently available over time to allow for long-range planning.	Yes	No[a]	No
6.	Disaster assistance programs, in the way they provide financial assistance, should help farmers withstand and recover from the effects of natural disasters.	Yes	Yes	Depends[b]
7.	Disaster assistance programs should have predictable annual costs.	Depends[c]	No	No
8.	Disaster assistance programs should meet their objectives at the lowest possible cost.	Depends[d]	Depends[e]	Depends[d]

[a] The Emergency Feed Program and the Emergency Feed Assistance Program are consistently available to producers to help them with long-range planning.

[b] Meets criterion only to the extent that loan principal is forgiven.

[c] Meets criterion to the extent that the program is run on an actuarially sound basis.

[d] Would meet criterion to the extent that programs were not subsidized. For crop insurance, incentives would be reduced to the extent that premiums reflected actual risks and that subsidization of high-risk participants by low-risk participants was minimized.

[e] Would meet criterion to the extent that losses are only partially compensated and that compensation for risky farming practices was prohibited.

Senator PRYOR. Bill Classen, Classen, I guess that is.

Senator HARKIN. Classen from Des Moines.

Senator PRYOR. Classen. Oh, my. Well, the Senator from Iowa has corrected me. He is the president of Rain and Hail Insurance Service Incorporated, and Ray Davis, from Potter, Nebraska, Senator Kerrey's constituent, and these gentlemen have cochaired the Commission for the Improvement of the Federal Crop Insurance Program. And any further introduction or elaboration on either of these gentlemen or both, we will turn over to Senator Harkin and Senator Kerrey, if you all would like to say a word about them in introduction.

Senator HARKIN. Well, Mr. Chairman, I would just say that Bill, as you said, was vice-chair of this Commission. He also was a member of the Commission. Both have extensive backgrounds in this area. Bill is also president of Agra-General Insurance Services and Agra-General Insurance Company, past president of the National Crop Services and presently vice-chair of the American Association of Crop Insurance, and they have done yeoman's work on this Commission. I met with them often in the past, and they bring a wealth of experience and knowledge to this table.

Senator PRYOR. Good. Thank you, Senator Harkin. Senator Kerrey, any further words of introduction for your——

Senator KERREY. Oh, just that if more than 3 of 26 of this Commission's recommendations had been implemented we might not have to have this hearing today.

Senator PRYOR. Well, we are very appreciative of both of you coming. You have a great wealth of expertise in this area. I wonder, one, if you have prepared statements that you would like to summarize and put the full body of your statement in the record? We would encourage you to do that if possible. So Mr. Davis, we will—excuse me—either one want to go first? Mr. Davis.

STATEMENT OF RAY DAVIS, COCHAIRMAN, COMMISSION FOR THE IMPROVEMENT OF THE FEDERAL CROP INSURANCE PROGRAM, WHEAT FARMER, POTTER, NE

Mr. DAVIS. I will go first.

Senator PRYOR. Mr. Davis.

Mr. DAVIS. I am the most nervous so I better get it out of the way.

Senator PRYOR. Well, you do not need to be nervous in this subcommittee.

Senator BOSCHWITZ. The Senator from Minnesota notices that the witnesses are from Nebraska and Iowa and Oklahoma and Iowa and Arkansas. Come the revolution, they will all be from Minnesota. [Laughter.]

Senator KERREY. Then you will show up on time. [Laughter.]

Senator BOSCHWITZ. But we welcome you, Mr. Davis, and Mr. Classen, and I am sure that you are going to be very helpful to us.

Senator PRYOR. Mr. Davis, thank you.

INTRODUCTION

Mr. DAVIS. Thank you, Mr. Chairman, distinguished Senators and guests. As you know, I am Ray Davis, a farmer from Potter, Nebraska, and I would like to state that my income comes essentially from farming. The gentleman sitting next to me is Bill Classen from Des Moines, Iowa, a crop insurance company executive who is also a farmer. We are the Cochairmen of the Commission for the Improvement of the Federal Crop Insurance Program. I will summarize part of the prepared statement Mr. Classen and I have submitted to the subcommittee.

Senator Boschwitz. Where is Potter?

Mr. Davis. Potter is now Potter-Dix because the girls and boys have both made it to the State basketball tournament. It is between Sidney and Kimball. It is in the western part of the State. It is 400 miles west of Omaha and 80 miles east of Cheyenne, Wyoming.

Senator Boschwitz. Well, it is out in the middle of nowhere. [Laughter.]

Senator Bond. Rudy, that is what we used to call Minnesota. [Laughter.]

Senator Boschwitz. That is a pretty fair statement, is it not, Mr. Davis?

Mr. Davis. When I was a boy, my grandfather used to say, "way out west where the hop toads wink, just a lonely country gink."

FUNDING OF THE 1991 PROGRAM

Mr. Chairman, before discussing the work of the Commission and its recommendations for improving the crop insurance program, we would like to call your attention to an urgent matter. Farmers need to know that adequate funding will be available for the continuation of the Federal crop insurance program during the 1991 crop-year. This matter needs to be resolved as quickly as possible. Producers of several commodities, such as wheat and citrus, will be making their final production plans for the 1991 crop-year during the next few months. These producers and their lenders need to know that crop insurance will be available for the 1991 crops.

At its February 1990 meeting, the Commission adopted a resolution encouraging each of the appropriate committees of Congress to express support for the continuation of the present program through the 1991 crop-year.

Mr. Chairman, the Nation's farmers need the assurance that the crop insurance program will be continued during the 1991 crop-year. We urge the subcommittee to support efforts to give our farmers that assurance.

WORK OF THE COMMISSION

I would now like to turn to the work of the Commission.

Beginning in March of 1989, the Commission held 14 public hearings throughout the United States. Using the testimony presented at the hearings, together with the experiences of the Commission members, the Commission developed an interim report in April 1989 recommending various administrative changes for immediate implementation by the FCIC, aimed at improving the program in the 1990 sales year. These changes were designed to foster increased participation by producers.

Following the completion of the April report, the Commission directed its efforts to the development of recommendations to effect long-term changes—changes that would improve program participation, streamline program procedures, and more clearly define the goals and objectives of the program so as to lessen, if not eliminate, the need for future ad hoc disaster assistance programs. The principal report, dated July 1989, is the product of this effort.

At meetings which the Commission held after the submission of the July report, we developed additional recommendations designed to improve the operation of the program and assist in retaining the participation gained during the 1989 crop-year.

RECOMMENDATIONS OF THE COMMISSION

All of the Commission's recommendations are aimed at providing better and more cost-effective Federal crop insurance for the Nation's farmers, with the ultimate goal of providing to them more equitable, efficient, and predictable protection from natural disasters.

Mr. Chairman, we would like to call to the subcommittee's attention the fact that, in addition to the specific recommendations set forth in the Commission's July 1989 report, the Commission agreed to include in the report, for consideration by Congress and the Federal Crop Insurance Corporation, an alternative proposal for a new crop insurance program. The provisions of that proposal are set out in appendix B of the report. The Commission, at its meeting in February 1990, reviewed the alternative program. Based on that review, the Commission recommends that Congress, in developing a crop insurance program based on sound insurance principles, give special consideration to the alternative program outlined in appendix B of the July 1989 report.

The vast majority of the witnesses at the Commission's hearings stressed the importance of providing better insurance coverage for agricultural producers. This is the key, Mr. Chairman, to improving program participation, as no issue is more important to producers than the availability of adequate insurance coverage.

Thus, the most important recommendation of the Commission, from the standpoint of the producer, concerns the issue of coverage. The Commission has recommended to Congress and the Secretary of Agriculture a set of voluntary yield plans with coverage based on: (1) the producer's Agricultural Stabilization and Conservation Service yield for ASCS program commodities and related commodities; (2) a county average yield for other commodities; and (3) a modified actual production history or APH program yield for all commodities. Under this coverage proposal, the APH yield cannot be lower than the producer's ASCS yield.

Mr. Chairman, the current actual production history, or APH, program has simply not provided adequate coverage to most producers. Producers in areas suffering several disasters in recent years have approved yields far below their ASCS yields and their normal production. The Commission recommends that yields used for insurance purposes be no lower than a producer's ASCS yield to ensure that producers have a floor below which insurance yields would not go.

CONCLUSION

As a wheat producer, I felt "first-hand" the effects of the 1988 drought. As a member of the Commission, I spoke with other producers who in 1988 saw some of their most fertile fields reduced to dust. Fortunately, Congress saw fit to provide ad hoc disaster assistance to help offset those losses. But I think that a cotton producer, Steve Verett, said it best when he told us at the Commission's initial public hearing in Lubbock, Texas, that "it is obvious that we can't depend on one-shot, band-aid disaster payments which may or may not be forthcoming. We need a Federal crop insurance program that will provide adequate protection at reasonable cost, year in and year out."

It is my firm belief that the success of the Federal crop insurance program, and the elimination of the need for ad hoc disaster assistance payment programs, are dependent on an effective and consistent insurance product. The Nation's agricultural producers need a disaster assistance program that is stable, consistent, and efficient. As a representative of the agricultural community, I believe that the Commission's recommendations for improving the Federal crop insurance program represent a superior blueprint for this type of disaster assistance program.

Mr. Chairman, I am honored to participate in the deliberations of this esteemed body, and I thank you.

I would like to yield to Mr. Classen for his summary.

Senator Pryor. Mr. Classen, you now have the floor. Thank you very much, Mr. Davis.

STATEMENT OF BILL CLASSEN, COCHAIRMAN, COMMISSION FOR THE IMPROVEMENT OF THE FEDERAL CROP INSURANCE PROGRAM, PRESIDENT, RAIN AND HAIL INSURANCE SERVICE, INC., DES MOINES, IA

Mr. Classen. Thank you, Mr. Chairman, and Senator Harkin, I appreciate your introduction. I did not know you knew how to say my name properly, but you do very well, and I appreciate that.

Senator Harkin. Well, that is all right. We can teach the rest of these people around the table to speak like Iowans here pretty soon.

Mr. Classen. Very good. Right, Senator.

Senator Pryor. If I might, Mr. Classen, if I could interrupt just for a moment—did I mispronounce?

Senator Harkin. No, you were right. Just keep going.

Senator Pryor. I am just going to call you Bill from now on.

Mr. Classen. I appreciate that, too, Senator. And members of the committee.

Senator Pryor. If I could interrupt for a moment, let me do this. I understand that we have a very fine colleague, former colleague of ours, who was with us for years in this room and knows as much about this farm bill as probably all the rest of us put together, and I understand this is someone who has been closely associated with your Commission, and that is Kellye Eversole. I believe Kellye is sitting here on the front row, and we appreciate Kellye being here today, and I know she has been invaluable to you throughout your debate on Federal crop insurance. We are proud to have Kellye here.

Mr. DAVIS. I had her name on my statement to introduce her, but she deleted it.

Senator PRYOR. Oh, no. She is a little shy. Now we look forward to your statement.

INTRODUCTION

Mr. CLASSEN. Senator, I appreciate your recognizing Kellye. She has done an excellent job, as has her staff.

I am not going to repeat my name, but we operate a managing general agency on behalf of the CIGNA Corporation Companies, the State Farm Property and Casualty Insurance Company, and the National Farmers Union Companies.

While I serve on the Commission as a representative of the crop insurance industry, I was reared on the farm and am still actively engaged in farming. I can, therefore, appreciate the comments of my colleague and friend, Ray Davis, as he described the importance of providing American farmers with a stable, consistent, and efficient program for disaster assistance. I, too, believe that with substantial improvement, the Federal crop insurance program can provide our Nation's producers with more equitable, efficient, and predictable protection from natural disasters. American farmers must have a viable risk management program. In my judgment, crop insurance is the only risk management program that will work effectively for American farmers. The General Accounting Office agrees, at least in part, with my judgment. As you gentlemen know, that Office issued a report in September of last year in which it concluded that crop insurance can provide disaster assistance more effectively than other programs. This afternoon, representatives of GAO sitting across from us, reiterated that conclusion.

With the implementation of the Commission's recommendations, I believe that Federal crop insurance can be tailored to meet each individual farmer's needs. Risk is the driving force behind the American free enterprise system, and farmers must be given the opportunity and flexibility to manage all of their risks. American farmers deserve to make a profit and they deserve to be given the opportunity to manage the risks of production loss due to natural disasters through a workable crop insurance program.

THE FEDERAL CROP INSURANCE ACT OF 1980

Prior to 1980, the Federal crop insurance program was simply ineffective. The Federal Crop Insurance Act of 1980 signaled a new beginning for the program. Aside from authorizing a major expansion of the program, the act authorized the involvement, to the maximum extent possible, of private, nongovernmental organizations in all aspects of the crop insurance program. After the enactment of the 1980 legislation, the Federal Crop Insurance Corporation established a dual system of delivering the program through the private sector. Private insurance companies and licensed agents and brokers have now become the primary marketing arm for Federal crop insurance policies. To make the direct Federal policies and the private, federally reinsured policies cost-competitive, the FCIC was also authorized to reimburse participating companies for their administrative expenses and most of their operating losses since those costs are not passed along to the policyholders participating in the program of direct Federal insurance.

The involvement of the reinsured companies and the master marketers in the program has made possible the degree of success that the program has experienced in the past few years. However, we all recognize that we still have a long way to go before American farmers have a stable, effective, and efficient crop insurance program.

The private reinsured insurance companies and master marketers are committed to achieving a completely successful risk management program for farmers. As Cochairman Davis stated, all the Commission's recommendations are aimed at this objective.

RECOMMENDATIONS OF THE COMMISSION

With the chairman's indulgence, I will highlight some of the more significant recommendations that are essential to the insurance industry if we are to have a successful program.

At each of the Commission's hearings, witnesses repeatedly stated the need to simplify the Federal crop insurance program. Many of the Commission's recommendations for simplifying the program were made in the interim report issued in April 1989, as they could be immediately implemented administratively. Several of those recommendations, however, deserve comment.

SYNCHRONIZATION OF FILING DATES

In the April report, the Commission recommended that all pertinent USDA commodity program and crop insurance dates be synchronized to the maximum extent possible. ASCS and FCIC reporting dates are often different, thereby creating confusion among producers. In some cases, producers believe they have filed the appropriate form in time, only to discover that they missed the deadline for crop insurance but not for ASCS programs. Having different dates for the filing of the same information for different USDA programs merely causes confusion and frustration among producers and agents. Eliminating these discrepancies will provide a much simpler program.

TIMELY ANNOUNCEMENTS OF PROGRAM PROVISIONS

Another recommendation, included in the interim report, that is essential to program simplification and critical to both producers and the insurance industry is that all Federal crop insurance information released by the FCIC—such as rates, rules, policy changes, and forms—be in place, for the entire upcoming crop-year, by an early date.

Private companies, organizations and individuals simply must have all program information in a timely manner. From the standpoint of our agents, without timely program information, they simply cannot adequately market the product.

RESTRUCTURING OF THE FCIC

Essential to the overall success of the Federal crop insurance program is the restructuring of the FCIC. The Commission believes that the efficiency of the program can be enhanced by, among other things, developing an improved and streamlined organizational structure for FCIC; establishing a committee to advise the board of directors of the Corporation; using outside contracting to the greatest extent possible; and enacting legislation to establish, over the long term, a new corporation to carry out the Federal crop insurance program.

To be responsive to the needs of producers, the FCIC must be able to act efficiently and responsibly. The present structure of the FCIC fails to recognize that the program is delivered entirely by private individuals, organizations and companies—master marketers and reinsured companies. If the two delivery systems are to be responsive to producers, the structure of FCIC must accurately reflect the strengths of the delivery system and the strengths of FCIC.

In many cases, expertise in resolving an insurance problem or in establishing a new program for a previously uninsured commodity lies outside the FCIC. In these instances, the FCIC should take advantage of this expertise by seeking advice from an advisory committee consisting of producers and representatives from the insurance industry and by contracting with private individuals, organizations, and companies for the appropriate functions and projects.

ALTERNATIVE PROGRAM

In his remarks, Cochairman Davis made reference to the alternative program outlined in appendix B of the Commission's July 1989 report. I would simply note that the alternative program contains significant and important proposals for the restructuring of the FCIC.

INTERRELATIONSHIP OF THE RECOMMENDATIONS

Many of the Commission's recommendations are interrelated. The implementation of the recommendations that directly affect agricultural producers, such as providing adequate coverage, are essential to the overall success of the Federal crop insurance program. At the same time, the recommendations that more directly address concerns of the insurance industry, such as providing for a more efficient structure for the FCIC, are also essential to the success of the program. The implementation of these recommendations will enable the two delivery systems to more efficiently deliver the insurance product to the Nation's agricultural producers. A healthy insurance industry is essential to the success of the Federal crop insurance program.

CONCLUSION

In conclusion, as members of the Commission, we are committed to the development of a sound, consistent, reliable, and efficient Federal crop insurance program. If crop insurance is to be the risk management tool of agricultural producers in the future, there is a critical need to substantially improve the current program from the standpoint of the producers, as well as the insurance industry.

Mr. Chairman, we believe that the Commission's recommendations will help establish a meaningful risk management program for our Nation's farmers. In my judgment, crop insurance is the only program that has the potential of one day being self-sustaining through a successful marriage between the Government and the private companies, organizations and agents.

Mr. Chairman, you and the members of the subcommittee are facing a major challenge in developing legislation to improve the Federal crop insurance program. However, we are confident that it is a challenge you will successfully meet. We commend your efforts to develop a meaningful risk management program for our Nation's farmers.

Mr. Chairman, this concludes our summary of the Commission's prepared statement. We will be happy to answer any questions.

Senator PRYOR. Let me ask you a couple quick questions and then I am going to yield to Senator Kerrey and Senator Cochran. By the way, I think what we will do is if we could get somebody to run our little lighting system here, we will have 5 minute rounds of questions, if that is agreeable with our colleague. What sort of support in the last 10 years have you received for basically the Federal crop insurance program from the U.S. Department of Agriculture on a scale of 1 to 10?

Mr. CLASSEN. I think I probably disagree a little bit with our GAO friends, Mr. Chairman. I think early on, because we started in 1981 as our first year, we had extremely good cooperation. I think as we have concluded the 1989 crop-year, we have had less cooperation from FCIC. It seems, as we have gone from year 1 to year 9, we have had less cooperation from the standpoint of being able to sit at a table with FCIC officials, as we are sitting here now, to determine what the problems are and how we could correct those problems.

Many times, it seems that our problems had to come back through you, Mr. Chairman, and the members of the subcommittee, and to the House Members. Things had to be extremely critical before we could get any attention from our FCIC friends. I do not think that we should have the problems today that we seem to have with the crop insurance program. I think it is totally unnecessary. I think they could have been corrected. I realize we have a Federal deficit. I realize we have a budget that we have to live with. Some of the earlier questions by some of your subcommittee members—regarding budgets and OMB and who really calls the shots—have to be looked at carefully. This is a program that you cannot start up today and close down tomorrow. It is a long-term program, Mr. Chairman, and the industry has invested over the 9 years, substantial amounts of money in equipment, facilities, and personnel to conduct a proper crop insurance program.

Senator PRYOR. Thank you very much. That was a fine statement. Mr. Davis, do you have any comments on that? Do you want to step into that thicket? If not, we will call on Senator Kerrey.

Senator KERREY. Mr. Chairman, I thank you. I actually would like to ask a question in between the two of you because it seems to me that what we have before us is a task and I think a majority of the full committee members are trying to figure out how to make the crop insurance program work. Essentially that means asking what kind of legislation and what sort of detail are we going to put together? Boy, that was quick.

Senator PRYOR. That was a quick question.

Senator KERREY. Boy, time flies when I am asking a question. What I am concerned about are essentially two separate categories. One is the management of FCIC and how we need to set this thing up so that we get taxpayer accountability and responsiveness, and the second is delivery. The second set of questions concerns delivery, and I would like to ask, Ray, either you or Mr. Classen, on the management side, have you any ideas for us at all on how we can put this together so that there is accountability, which I clearly want on behalf of the taxpayer but also so that you do not have to come back to this committee or to the House committee as well to get some sort of action? And then for Mr. Harman, is it possible for GAO, and perhaps you have already done it, to do some sort of evaluation for us quickly of the recommendations that were made last year so that we can factor that analysis into the development of the bill itself?

Mr. DAVIS. Well, on the management of the program, I would defer to my colleague. He is more involved in administrative matters. I could relate a little bit. I said that most of my income was from farming, which is true. I do some adjusting. And I have adjusted for both Federal crop and American Ag, which is a reinsurer. And it is quite an experience. It sounds pretty easy to adjust crops when you are sitting here at the table. When you get out in the field and you tell a farmer that he has half a bushel left there, he will look you straight in the eye and he will say "how am I supposed to harvest a half a bushel?", and you will say, "well, I am sorry, Mr. Farmer, but I have to deduct this from your payment." You can see how an adjuster is only human.

When the adjuster is out there and the farmer has a loss, he wants to get him paid. So you can see where there may be some slippage. And we need to tighten controls on adjusters. I have seen adjusters in the field just drive by a field and adjust it. I am a certified adjuster. I am certified in seven crops, and I would not even begin to tackle something like sugar beets if I was not certified in it. It would just be impossible.

Mr. CLASSEN. Senator Kerrey, from the standpoint of taxpayer accountability, I do not think this is an impossible task at all. As I said a bit earlier, first of all, we went into this program in good faith, from the private industry side, with the Federal Government. When you do that, I guess you could call it a marriage, or if you like, a cooperation of the private/Government sectors, whichever sounds better.

But when you do that—in my estimation—there must be give and take on both sides. From a management standpoint, there has to be accountability of the taxpayers' dollars. There is just no question about that. And I think the industry has a very, very high regard for that. From the Government side, we see rules in place that they have to observe. Many times we are not able to use common sense. We have to go by section, paragraph, and page number on an insignificant matter even though you are going to spend $10,000 of the taxpayers' money. We do not think it has to be that way.

I think we need to restructure the FCIC to develop a reinsurance oversight approval organization and move this program to the private sector on a risk-bearing basis. Now, we have asked for this. In negotiating with the FCIC, we have had many, many meetings, and we could have saved the expense money because nothing happened. There was no response. Gentlemen, that is what we have been fighting. I am not here to complain. I am, hopefully, putting facts on the table. And I think the Commission will back up what I am saying. We have to get over to a risk-bearing basis, and as Senator Bond from Arkansas——

Senator PRYOR. Missouri.

Mr. CLASSEN. I am sorry. Senator Pryor, I am sorry.

Senator PRYOR. You are insulting the people of Missouri when you—— [Laughter.]

Mr. CLASSEN. I apologize, Senator Pryor.

Senator PRYOR. Thank you, sir. No, that is quite all right.

Mr. CLASSEN. At one time I had the Iowa, Missouri-Arkansas office, and so I always kind of related those two States together.

Senator PRYOR. Right.

Mr. CLASSEN. Senator Bond has related some very radical adjustment problems. In private conversation with Senator Bond, he has stated that if you are going to foolishly distribute taxpayers' money, he is not going to go for this crop insurance program. And, I think that is kind of what he was saying earlier this afternoon. We have pleaded with the FCIC to structure the program so that the companies can carry risk. Now when you do that, you also must go back to the Commission's appendix B program that we mentioned earlier. It will be talked about more. Under the proposal, the rates would become actuarially sound by eliminating the expense reimbursement and adding it into the rate structure. Now this is radical, but this is the way a private insurance program works.

The companies would be willing then to take a high number of percentage points of risk. By the same token, they want to be able to recoup the losses that they may have. Now, when you do this, I hope that would satisfy Senator Bond. The companies would be spending their own money—I'd have to dig into my pocket and pay the policyholder. It has to be on a fair basis according to the insurance policy contract. No more, no less, and that is how the insurance industry operates. I see no reason why this program could not be structured on that basis. However, there probably will have to be some factor involved to account for social policy aspects of the program, and possibly a catastrophe factor for disaster years, such as 1988.

Senator PRYOR. Thank you.

Mr. CLASSEN. Senator Kerrey, I do not know if I answered your question or not.

Senator KERREY. Well, you answered part of it. Yes, I have the information that I need from your answer.

Mr. CLASSEN. Thank you.

Senator KERREY. On the GAO side, Mr. Harman, if you have done any evaluations or if it is possible for you to do some rather quick evaluations of the proposals that have been made, I would like to get them.

Mr. **HARMAN**. I think certainly we could do some of that. Of course, what we are able to do would depend upon the time we have to do it. But I would tend to agree with much of what they have said.

Senator **KERREY**. I always thought that the time required to get the job done sort of expanded with the time allowed to do the job. That is not true?

Mr. **HARMAN**. That is not true. [Laughter.]

And I know we are certainly aware of the work the Commission has done. We followed the recommendations that they have made. There are some that we probably will have some problems with, particularly anything that has to do with reestablishing countywide averages would perhaps probably raise some concerns for us to the extent it gets involved in adverse selection again. But we could do some of that, and a great deal of what has been said, I think has to be done. We have to make this a true insurance program. But we would be able to do that, and we can get with your staff and work out the arrangements for that.

Senator **PRYOR**. Thank you, Mr. Harman. Senator Cochran.

Senator **COCHRAN**. Thank you, Mr. Chairman. I am just curious if we do implement a proposal such as you have made today to convert the program into a true insurance program or put it on a more businesslike business which is what I gather from your suggestions, what do you estimate the cost to the Government would be of that kind of program?

Mr. **CLASSEN**. Senator Cochran, we have a gentlemen here to specifically answer your question. Dr. Stansbury will come forward and give you a response.

Dr. **STANSBURY**. Senator Cochran.

Senator **COCHRAN**. Hello, Dale. Welcome.

Dr. **STANSBURY**. My name is Dale Stansbury and I am a consultant doing research for the Commission. What happened, Senator Cochran, is the costs that are currently incurred by the Government as unintended subsidies become purposeful additions to the premium. So it is basically a transfer of what the costs currently are into an open, explicit statement of costs. For instance, if you had a premium of $1,000 under the current program, you would add $360 for delivery costs, $20 for claims adjustment, and $560 for average excess losses. And that gives you an average of about $1,940. If you transfer all the subsidies to the premium and you add in the cost that the insurers are going to assume because of the risks that they take, the numbers would come out to be about $1,955. So it basically is merely bringing the numbers to the table and assigning them in the beginning rather than at the end.

Senator **COCHRAN**. What would you think about supplementing the crop insurance program with a predictable disaster relief program rather than having an ad hoc response by Congress every time there is a major disaster, much like we have in the Small Business Administration administered program for hurricane victims and others who do encounter disasters in other ways that are not just strictly related to agriculture? Is that something that you considered when you were reviewing this?

Mr. **Classen**. Senator, I think that that would take some work with many people. I would think that it could be incorporated in one total program so that you folks would not be called on to deal on an ad hoc basis with the problems that we have had as a result of natural disasters. We certainly agree that there should be one program and not two programs. If we channel the resources that we have into one good program, I would think that there should be a mechanism built into the legislation and into the new program that could handle a catastrophe type situation.

Senator **Cochran**. Well, I am reminded, Mr. Chairman, of our situation, you know, on the gulf coast we are hit with hurricanes from time to time, and back in the early days whenever you had a really major catastrophe—Hurricane Camille is an example that comes to mind—legislation was enacted by the Congress to provide special benefits and relief to the disaster victims in Mississippi and elsewhere who were victimized by that storm. And then you remember Hurricane Agnes came along later on, and that got the attention of people farther north because it plowed a furrow all the way up to Pennsylvania, at least with a deluge of rain and you had massive flooding problems, and the Congress responded with an ad hoc, special relief measure that provided benefits.

But it occurred to the Congress then that this was going to get kind of tiresome and that what we were also going to do was see that the Congressmen and Senators from the disaster areas wanted to do just a little bit better the next time, provide just a little greater sensitivity in the form of benefits, and so the costs were getting to the point where that became a problem. And to avoid that, Congress enacted sort of a basic standard disaster relief policy and program, and now when you have a disaster, as we just had in our State with some floods and all, you are declared a disaster area and you have this prescribed benefit structure and it is not perfect, and there are a lot of problems with it still. But nonetheless, there is a predictable level of benefits. They are all described in the law. It seems to me that we may be at that point in agriculture where rather than try to enact a specific remedy each time there is a disaster, a drought up in the Dakotas and Nebraska; we had floods last year in the South; we had to come up with a benefit program and try to identify the money available from the savings that were going to be realized in the changes in prices and the other impacts that could be attributable to the drought.

It is sort of a crazy way of going about it, just to be honest about it. And, you know, some people got benefits. Some people did not. I just think we do need to have a standard policy established by this committee, and this is a good year to do it. There is no need to wait any longer. We have the benefit of this Commission's report. The administration has some ideas. I hope, Mr. Chairman, we can resolve this issue. I think we need a crop insurance program, but I do not think we need one that is abused like this one is. We do not need people farming the crop insurance program, and I think we have that. I do not know whether GAO has made information like that available to this committee, or whether you tried to identify fraud of that kind.

But I think there is some of that out there. The farmers in my State tell me they know about it. But then you have also the situation where the insurance premiums are so high for what you might get in the form of a benefit that so-called good farmers, those that are not going to farm the program, are not buying the insurance. Only 20 percent of the eligible land in my State is covered by crop insurance, and this has been since 1981. You would think that the program would be attractive enough so that in a State like Mississippi where we are very dependent upon agriculture as part of our State's economy that more than half, you would think, of the farmers would be involved in participating in the crop insurance programs. So it does need fixing, and I just want to thank Mr. Davis and Mr. Classen and others, Mr. Harman, who are here, helping us understand this better, and I am sorry, I have run over my 5 minutes. Thank you, Mr. Chairman.

Senator PRYOR. A very good statement, Senator Cochran, and I think you have expressed the sense of a lot of us around this table. Senator Kerrey, do you have further questions?

Senator KERREY. No, I do not.

Senator PRYOR. I would like to thank very much our two witnesses today. I would also like to request that we may from time to time in the next week or 10 days have further questions. You have built in a tremendous amount of expertise and we would like to delve into some of that knowledge and expertise, and I am sure there may be some written questions to follow on from various members of the committee. We are very, very grateful for your participation. We are grateful as always to the General Accounting Office. We thank the three of you, and we will now move to our next panel. Thank you.

Mr. CLASSEN. Senator, if I may——

Senator PRYOR. Yes, sir.

Mr. CLASSEN. We certainly would be available. We have a broad experience base on the Commission. Any time that you would like any help, we would be more than pleased to assist you.

Senator PRYOR. We may not only want to send you a question by mail—by the way, the stamp is going up to 30 cents, so it may be cheaper just to fly you back here and let you visit with us in person again. We thank you very, very much, all of you.

Mr. CLASSEN. Thank you.

[The prepared joint statement and attachments A–D of Mr. Davis and Mr. Classen follow:]

COMMISSION FOR THE IMPROVEMENT OF THE FEDERAL CROP INSURANCE PROGRAM

TESTIMONY

For Release
On Delivery
2:00 p.m. EST
Tuesday
March 6, 1990

Improving the Federal Crop
Insurance Program

Statement of
Ray Davis and Bill Classen, Co-Chairmen
Commission for the Improvement of the
Federal Crop Insurance Program

Before the
Subcommittee on Agricultural Production and
Stabilization of Prices
Committee on Agriculture, Nutrition, and Forestry
United States Senate

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Mr. Chairman and Members of the Subcommittee:

My name is Ray Davis. I am a farmer from Potter, Nebraska. The gentleman next to me is Bill Classen from Des Moines, Iowa, a crop insurance company executive who is also a farmer. We are the Co-Chairmen of the Commission for the Improvement of the Federal Crop Insurance Program. We are accompanied by Ms. Kellye Eversole, the Executive Director of the Commission, Carl Rose, the Commission's special counsel, and Dale Stansbury, the Commission's independent research consultant.

We are pleased to appear today to discuss the Commission's findings and recommendations on ways to improve the Federal crop insurance program. We also want to discuss briefly a urgent matter that needs to be addressed as quickly as possible by Congress and the Administration. In light of the Administration's proposal to repeal the Federal Crop Insurance Act, farmers need to know that adequate funding will be available for the continuation of the crop insurance program during the 1991 crop year.

Introduction

Farming is an exceptionally high-risk undertaking. In addition to the economic uncertainties caused by fluctuating prices for agricultural products, farmers face a variety of uncontrollable and unpredictable natural hazards that can prevent the planting of crops or destroy planted crops and other property. Historically, 1 out of every 12 acres planted is not harvested because of adverse weather or other natural disasters.

Natural disasters are random events. It is inevitable that they will strike some segment of the population, that some victims will not be able to finance losses from personal resources, that private insurers will not always be able to insure against such losses, and that some victims will be financially crippled. Agriculture is unique among the Nation's businesses in that farming is constantly susceptible to natural disasters.

Growing crops represent a major investment for the farmer. Considerable capital is needed to buy the machinery, fuel, fertilizer, seed, pesticides, and other requirements of modern commercial agriculture, the costs of which escalate each year.

In most cases, farmers have to borrow money to plant their crops. Farmers often are unable to repay their loans and have difficulties in securing adequate credit to finance future crops when unavoidable natural disasters result in losses of production. The complete loss of a single crop due to the occurrence of a natural disaster can drive a person out of farming. Where there are widespread crop losses in consecutive years, a not uncommon occurrence, financial distress among farmers increases. This, in turn, affects the financial well-being of our Nation's lending institutions and commercial, agricultural businesses.

Because of the adverse effects of natural disasters, it is critical that the government provide some form of a disaster protection program to enable farmers to pay their bills and remain in farming. In some cases, the assistance that has been provided by our government is the only means by which a farmer remains in business. In addition, the benefits of a disaster relief program extend far beyond the affected agricultural producer. The income provided enables farmers to continue to pay their debts and make new purchases, thereby contributing to the stability of the local economy. In addition, the benefits ensure the maintenance of agriculture's productive capacity, thereby ensuring that America's consumers continue to receive an abundant supply of food and fiber products at reasonable prices.

It is critical that American agricultural producers have a consistent, reliable, and efficient disaster assistance program. To be consistent, the program should ensure that victims of similar natural disasters experiencing similar losses be accorded the same benefits and bear a similar share of the costs. In addition, to be consistent, the generosity of Federal disaster relief should vary with the severity of the disaster losses, not with the terms under which the programs are subsidized.

In the past, major changes in disaster assistance policy have often occurred in the wake of widespread natural disasters. During these periods, assistance has often been generous even though individual losses were less, in many cases, than those of an isolated disaster. For isolated cases, the terms of disaster assistance have often been less generous or not available at all. The degree of Federal disaster assistance has varied from year to year and from commodity to commodity due to ad hoc changes in assistance policy. These changes create inconsistencies and violate common sense notions of equity. The effects of a complete crop loss do not vary--they are devastating to the individual involved and the widespread occurrence of a natural disaster does not mitigate these effects.

The Federal Crop Insurance Act of 1980

The Federal Crop Insurance Act of 1980 signaled a new beginning for the Federal crop insurance program with the hope that crop insurance would ultimately replace the need for other forms of disaster assistance. That legislation authorized the Federal Crop Insurance Corporation to provide insurance coverage for every commodity produced commercially in the United States.

The Act required the FCIC to offer various levels of coverage, including coverage of 50 percent and 75 percent of the recorded or appraised yield. In addition, the Act provided for the FCIC to pay 30 percent of a producer's premium on coverage up to a maximum of 65 percent of the recorded or appraised average yield.

The 1980 Act also authorized the involvement, to the maximum extent possible, of private, nongovernmental organizations in all aspects of the crop insurance program. After the enactment of the 1980 legislation, the FCIC established a dual system of delivering the program through the private sector. Private insurance companies and licensed agents and brokers have now become the primary marketing arm for Federal crop insurance policies. To make the direct Federal policies and the private, federally reinsured policies cost competitive, the FCIC was also authorized to reimburse participating companies for their administrative expenses and most of their operating losses since those costs are not passed along to the policyholders participating in the program of direct Federal insurance.

Despite the introduction of a premium subsidy and the rapid expansion of eligible commodities and eligible acres under the Federal crop insurance program, participation levels have not grown as anticipated. When the 1980 Act was passed, policymakers envisioned a participation rate approaching 50 percent of planted acreage by the end of the decade. Although coverage expanded from 26 commodities in 1980 to almost 50 commodities in 1988, participation did not reach the anticipated levels.

Mr. Chairman, preliminary estimates indicate that participation levels in 1989 were substantially above the levels in 1988. Undoubtedly, much of the increase in participation is due to the requirement under the Disaster Assistance Act of 1988 that certain producers receiving assistance under that Act purchase crop insurance for the 1989 crops.

Establishment of the Commission

In 1988, this country endured one of the most severe droughts on record, ranking fourth in terms of total area covered by extreme or severe drought. For the Nation's corn belt, only the droughts of 1934 and 1936 covered more area than the drought of 1988. As a result, Congress was called on to provide approximately $3.5 billion in emergency disaster relief, while the Federal Crop Insurance Corporation was incurring $617 million in losses. Since 1981, the cost of disaster payment programs has soared over $5 billion, averaging approximately $565 million per year. The Disaster Assistance Act of 1989 which is estimated to provide $900 million in additional relief continues this trend.
If only the years 1981, 1986, and 1988--when nationwide disaster payment programs were in effect--are considered, the average cost of such programs is approximately $1.6 billion per year.

During the consideration of the Disaster Assistance Act of 1988, as noted by Congressman Ed Jones, "questions were repeatedly raised about why more producers weren't insured under the Federal Crop Insurance Program." Congressman Jones then said:

> After all, in 1980 Congress completely overhauled the program to include coverage on virtually all crops in every county.
>
> However, the sad fact is that only about 25 percent of the acreage eligible for insurance coverage currently is enrolled in the program. This level of participation simply is not adequate enough to address the financial consequences of a disaster like we experienced this year. Nor is producer participation in the program sufficient to forestall the political pressures that always come to bear when natural disasters strike a wide path, especially in an election year. (Statement by Congressman Ed Jones during consideration of the Federal Crop Insurance Commission Act of 1988. See 134 Cong. Rec. H8230 (daily ed. Sept. 26, 1988).)

Thus, in the wake of the 1988 drought, Congress enacted the Federal Crop Insurance Commission Act of 1988, which established an advisory panel to study the Federal crop insurance program. Specifically, the purpose of the Commission established by the 1988 Act is to ensure a thorough review of the Federal crop insurance program and the development of recommendations for such changes as are needed to improve the program so as to lessen, if not eliminate, the need for additional disaster payment programs while providing to producers of agricultural commodities more equitable, efficient, and predictable protection from natural disasters.

The Commission is composed of 25 members with 4 of them being non-voting members: the Chairmen and ranking minority members of the congressional agriculture committees, or their designees. Of the 21 voting members, 10 represent major agricultural interests, 10 represent various aspects of the crop insurance industry, and the final member is the manager of the Federal Crop Insurance Corporation. There is one vacancy on the Commission at the present time.

Under the statute, the Commission is specifically charged with the responsibility of studying and determining why participation in the Federal crop insurance program has not reached the levels of participation that were anticipated when the Federal Crop Insurance Act of 1980 was enacted.

Funding of the 1991 Program

Mr. Chairman, before discussing the work of the Commission and its recommendations for improvements in the crop insurance program, we would like to call your attention to an urgent matter that needs to be addressed by Congress and the Administration. Farmers need the assurance that adequate funding will be available for the continuation of the Federal crop insurance program during the 1991 crop year. This matter needs to be resolved as quickly as possible. Producers of several commodities, such as wheat and citrus, will be making their final production plans for the 1991 crop year during the next few months. These producers and their lenders need to know whether crop insurance will be available to assist producers in managing the risks involved in the production of 1991 crops.

Ordinarily, adequate funding to operate the crop insurance program is assumed, and farmers rely upon the continuation of the program in making their plans for the next crop year. However, the Administration, in submitting its proposed budget for fiscal year 1991, announced that it plans to seek termination of the current crop insurance program effective at the end of the 1990 crop year. As a result, much confusion has been created in rural America. Many existing policy holders are concerned about how the Administration's announcement will affect their farming operations. Other producers have been reluctant to enroll in the program this year, not knowing the status of the program.

At its February 1990 meeting, the Commission determined that immediate action needs to be taken to assure farmers that crop insurance will continue to be available for their 1991 crops. Therefore, the Commission adopted a resolution encouraging each of the appropriate committees of Congress to express support for the continuation of the present program at a level adequate to ensure continued service to producers through the 1991 crop year. The resolution also (1) urges the Secretary of Agriculture to take immediate action to ensure that the 1990 crop insurance program and associated agreements with the delivery systems are carried forward without change for the 1991 crop year; (2) urges Congress to adopt a resolution requesting the Secretary to take action to ensure the continuation of the present program until such time as Congress may see fit to enact legislation providing for changes in the program; and (3) urges Congress and the Secretary to take all appropriate action as expeditiously as possible to ensure the continuation of the crop insurance program through the 1991 crop year to prevent the cancellation of continuous crop insurance policies. The Commission's resolution urges the Secretary to complete such action by May 1, 1990.

Mr. Chairman, the Nation's farmers need the assurance that adequate funding will be available for the continuation of the crop insurance program during the 1991 crop year. We urge the Subcommittee's support of efforts to give our farmers that assurance.

Work of the Commission

We would now like to turn to the work of the Commission.

During March and April of 1989, the Commission held 14 public hearings throughout the United States to allow producers, agents, and other interested parties an opportunity to discuss the problems and future direction of the Federal crop insurance program. Using the testimony presented at the hearings, together with the experiences of the Commission members, the Commission developed two reports that include recommendations aimed at providing better and more cost-effective Federal crop insurance for the Nation's farmers.

In April 1989, the Commission submitted an interim report to the congressional agriculture committees and the Secretary of Agriculture. The report sets forth the Commission's findings and recommendations for immediate administrative improvements in the Federal crop insurance program that it believes would foster increased participation by farmers. The Commission's findings and recommendations fall into four general categories: (1) increased responsiveness to producer needs; (2) broadening participation; (3) program simplification; and (4) improvement of delivery system performance. A summary of the recommendations contained in the Commission's interim report appears at the end of this statement as Attachment "A".

On the whole, the response by the FCIC to the Commission's suggestions for administrative changes in the program has been good. The FCIC has agreed to partially implement 22 of the 26 recommendations in the interim report. However, the FCIC did not elect to implement the Commission's recommendation regarding two alternative yield coverage plans for the 1990 crops, which would, in the Commission's judgment have a great effect on increasing participation in the program.

In July 1989, the Commission submitted its principal report to the congressional agriculture committees and the Secretary of Agriculture. In addition to recommendations for administrative improvements in the Federal crop insurance program, this report includes recommendations for legislation. The recommendations included in this report fall into four general categories: (1) increased responsiveness to producer needs; (2) broadening participation; (3) program simplification; and (4) improved program administration. A summary of the recommendations contained in the Commission's principal report appears at the end of this statement as Attachment "B".

In the April report, the Commission noted its belief that the enactment of the Federal Crop Insurance Commission Act of 1988 demonstrated a serious commitment by Congress to a more effective Federal crop insurance program. As stated in that report and in the July report, the Commission believes that support by Congress and the Department of Agriculture is essential if crop insurance is to become the major risk management tool of agriculture insofar as natural disasters are concerned.

Recommendations of the Commission

While we do not attempt to address in this statement each of the Commission's recommendations, we would like to highlight the more significant recommendations. At the outset, Mr. Chairman, we would like to call to the Subcommittee's attention the fact that, in addition to the specific recommendations set forth in the Commission's July 1989 report, the Commission agreed to include in the report, for consideration by Congress and the FCIC, an alternative proposal for a new crop insurance program. The provisions of that proposal are set out in Appendix B of the report. The Commission, at its meeting in February 1990, reviewed the alternative program. Based on that review, the Commission recommends that Congress, in developing a crop insurance program based on sound insurance principles, give special consideration to the alternative program outlined in Appendix B of the July 1989 report. A summary of the alternative program appears at the end of this statement as Attachment "C".

1. Increasing Responsiveness to Producer Needs

The principal objective of the Commission in developing its recommendations was to address the specific concerns of agricultural producers. Thus, the Commission included in the interim and principal reports a number of recommendations aimed specifically at increasing the program's responsiveness to producer needs. The Commission believes it imperative that every action be taken that would, at a minimum, maintain participation in the program at the 1989 levels.

In that regard, as stated in the Commission's principal report, "No single issue is more important to producers than their belief that they are being offered adequate insurance coverage on their commodities." The vast majority of the witnesses at the Commission's hearings stressed the importance of providing better insurance coverage for agricultural producers. The Commission believes that better coverage is the key to improving program participation. Regardless of the other improvements that may be made to the Federal crop insurance program, if insurance coverage is not improved, the majority of the producers simply will not participate in the program.

The Commission made a number of recommendations designed to improve the insurance coverage of agricultural producers. The most important of these is the recommendation regarding insurance yield plans. In its principal report, the Commission recommends that coverage be based on one of the following voluntary yield plans: (1) the producer's Agricultural Stabilization and Conservation Service yield for ASCS program commodities; (2) a county average yield for other commodities; and (3) a modified actual production history program (APH) yield for all commodities, and for ASCS program commodities, the APH yield would not be lower than the producer's ASCS yield.

The current APH program has simply proven to be too cumbersome to interest certain producers in many areas and has resulted in low insurance yields in areas that have experienced repeated disasters in recent years. Producers of major commodities often do not have 10 years of certifiable yield records. In such instances, the FCIC uses a percentage, usually less than 100 percent, of the ASCS yields (T-yields) for years without records that, when averaged with the producer's proven yields, often result in an insurance yield much lower than the producer's normal production. In addition, when yields from disaster years are included in the average, insurance yields can drop dramatically in areas that have experienced several disasters during the 10-year period. Since insurance coverage, at most, is only available for 75 percent of a producer's yield, the use of T-yields or yields from disaster years can render the insurance offer relatively meaningless to the producer.

The Commission believes that a "floor" below which yields cannot go and the elimination of T-yields, except when ASCS yields are the result of combining yields from irrigated and non-irrigated acreage, are essential to providing adequate coverage to agricultural producers. Permitting producers to base their yields on their own ASCS yields will also greatly simplify the program for most producers.

To ensure that the ASCS yields accurately reflect actual production and different practices, the Commission recommends that ASCS yields be revised, for crop insurance purposes. Because ASCS yields have been frozen since 1985, these yields generally understate the producer's actual potential production.

Insurance coverage is based on a producer's yield and the price election level chosen. During the hearings, producers also requested that price election levels more accurately reflect the market value of the commodities produced. The Commission therefore recommends that the FCIC establish a maximum price election level based on one of the following methods: (1) a futures market-based price election level, (2) a price election level based on the contract price of a commodity, (3) a projected market price at harvest time, and (4) a price election level based on the total economic cost of production of the commodity. The Commission also recommends that the maximum price election level be not less than the projected market price at harvest time. By establishing a maximum price election level, producers would have the option of selecting the level that best represents their own individual needs, and, when combined with the recommendation for determining yields, producers should be able to individually tailor their insurance coverage to their farming operations.

In determining coverage, the acreage included in the insurance unit is critically important. An insurance unit is all or that portion of the insured's farm acreage that is taken into consideration when determining coverage and when settling claims for losses. The Commission recommends that insurance units be standardized within regions for ASCS program commodities and soybeans, that units be not larger than the acreage included in one ASCS farm serial number, and that irrigated and non-irrigated acreage be in separate units. In the interim report, the Commission also recommended that producers be permitted to exclude high risk land from their insured acreage.

A large number of witnesses at the Commission's hearings expressed the need for a coverage level higher than 75 percent of yields. The Commission believes providing coverage up to 85 percent of yields should be tested and therefore recommends the enactment of legislation to require the FCIC to implement a pilot program that would permit producers to purchase coverage equal to 85 percent of yields.

2. Broadening Participation

While all of the Commission's recommendations are designed with the goal of improving the Federal crop insurance program and attracting greater program participation, the Commission has made a number of recommendations that it believes will specifically improve participation.

The cost of insurance coverage is an important factor to producers as they decide whether to purchase crop insurance. During the Commission's hearings, numerous witnesses recommended that the 30 percent premium subsidy be applied equally to all coverage levels as the relative cost of coverage based on 75 percent of yields is exorbitantly high since the premium subsidy is only applied to coverage levels up to 65 percent of yields. The Commission recommends that the 30 percent subsidy be provided for all coverage levels up to 75 percent of program yields.

Participation levels for the 1989 crop year rose substantially due to the provisions included in the Disaster

Assistance Act of 1988 that required certain producers to purchase crop insurance for the 1989 crops. Unless the program can be significantly improved, many of these new participants are likely to leave the program. In an attempt to solidify the participation of these participants until all of the Commission's recommendations can be implemented and a more marketable program is in place, the Commission recommends that a temporary, additional subsidy for all coverage levels up to 65 percent of approved yields also be offered to producers.

For the first year only, the supplemental subsidy would be 20 percent. The supplemental subsidy, to be phased out over a 5-year period, would, for the first year, result in a temporary, 50 percent subsidy for the levels of coverage up to 65 percent of approved yields. The supplemental subsidy, reduced by 4 percentage points each year, would be 16 percent, 12 percent, 8 percent, and 4 percent for the second, third, fourth, and fifth year, respectively.

Participation levels should increase dramatically, particularly at the lower coverage levels, and premium rates should improve as a result of the expected increase in participation in low-risk areas. When implemented along with the Commission's recommendations to improve approved yields, this increased subsidy should greatly lessen, if not eliminate, the need for other forms of disaster assistance.

While the adoption of this recommendation would require an increase in the Federal crop insurance program's budget, the Commission believes that this would be justified, and more than offset, if it were to result in significantly lessening, if not eliminating, the need for the ad hoc disaster assistance programs that have cost a total of $4.7 billion since 1983, excluding the disaster assistance provided to livestock producers.

Despite the requirement for certain recipients of assistance under the Disaster Assistance Act of 1988 to purchase crop insurance for the 1989 crop and the provisions included in the Disaster Assistance Act of 1989 that provide greater benefits to producers who purchased crop insurance, we respectfully suggest that many of the signals Congress and the Administration have given over the past few years have tended to discourage participation. Often, producers who purchased crop insurance had their benefits under various other agricultural programs reduced or limited precisely because they had purchased crop insurance. This tends to give the Federal crop insurance program a bad image, and many producers do not purchase crop insurance because they believe their benefits under other programs may be reduced. The Commission therefore recommends that Congress and the Administration ensure that no agricultural program, including disaster assistance programs, reduces or limits the benefits of the program due to a producer's receipt of Federal crop insurance indemnity payments. If crop insurance is to replace the ad hoc disaster programs of the past, consistent incentives must be developed to encourage producers to cover their production risk through crop insurance. Consistent Congressional and Administration support is essential to achieving this goal.

3. Program Simplification

At every one of the Commission's hearings, witnesses repeatedly stated the need to simplify the Federal crop insurance program. Chief among the methods expressed for simplifying the program was the need to express insurance coverage in terms of a dollar amount of coverage per acre. The Commission therefore recommends that the presentation of the insurance guarantee be changed to a dollar amount of coverage per acre. When combined with the Commission's recommendation on establishing a maximum price election level and permitting the producer to select any level up to the maximum, producers would be able to choose any dollar amount of coverage per acre up to a maximum dollar amount of coverage per acre based on the producer's yield and the maximum price.

The majority of the Commission's recommendations for simplifying the program were made in the interim report as they could be immediately implemented administratively. Several of those recommendations, however, deserve comment.

In its interim report, the Commission recommended that all pertinent USDA commodity program and crop insurance dates be synchronized to the maximum extent possible. ASCS and FCIC reporting dates are often different, thereby creating confusion among producers. In some cases, producers may believe they have filed the appropriate form in time, only to discover that they had missed the deadline for crop insurance but not for ASCS programs. Having different dates for the filing of the same information for different USDA programs merely causes confusion and frustration among producers and agents. Eliminating these discrepancies will provide a much simpler program.

Another recommendation included in the interim report that is essential to program simplification and critical to both producers and the insurance industry is the Commission's recommendation that all Federal crop insurance information released by the FCIC--such as rates, rules, policy changes, and forms--be in place, for the entire upcoming crop year, by an early date.

4. Improved Program Administration

There have been many references to abuse in the Federal crop insurance program. It has been said that some farmers are "farming the program" by using various means to collect insurance benefits without any real intention to produce a crop. While the percentage of producers who abuse the program in this manner is very small, the effects on all producers are significant. Not only is the integrity of the program and the agricultural community affected, the losses that occur as a result of intentional actions ultimately lead to higher premium rates for honest, hardworking farmers. Producers who abuse the program should be penalized for their actions and prevented from repeating the action. To address this problem, the Commission recommends that the FCIC be authorized to require participants to provide Social Security numbers, or individual tax identification numbers, that would assist in developing a tracking system to identify and monitor individual producers who abuse the program.

In its interim report, the Commission recommended that the FCIC establish a periodic performance rating system for the operation of the reinsured companies and master marketers and the individual functions performed. In addition, the Commission recommended that the FCIC develop mutually agreed upon standards of performance for reinsured companies and master marketers. As in the case of the recommendation for the development of a producer tracking system, these recommendations--if implemented--will help to ensure that reinsured companies and master marketers who abuse the program can be identified and eliminated from the program.

Essential to the overall success of the Federal crop insurance program is the need for restructuring the FCIC. The Commission believes the efficiency of the program can be improved by, among other things, developing an improved and streamlined organizational structure for the FCIC; establishing a committee to advise the Board of Directors of the Corporation; using outside contracting to the greatest extent possible; and enacting legislation to establish, over the long-term, a new corporation to carry out the Federal crop insurance program.

To be responsive to the needs of producers, the FCIC must be able to act efficiently and responsibly. The present structure of the FCIC fails to recognize that the program is delivered entirely by private individuals, organizations, and companies--master marketers and reinsured companies. If the two delivery systems are to be responsive to producers, the structure of the FCIC must accurately reflect the strengths of the delivery system and the strengths of FCIC.

In addition, in many cases, expertise in resolving an insurance problem or in establishing a new program for a previously uninsured commodity lies outside the FCIC. In these instances, the FCIC should take advantage of this expertise by seeking advice from an advisory committee consisting of producers and representatives from the insurance industry and by contracting with private individuals, organizations, and companies for the appropriate functions and projects.

Conclusion

All of the recommendations of the Commission are aimed at providing better and more cost-effective Federal crop insurance for the Nation's farmers with the ultimate goal of providing farmers more equitable, efficient, and predictable protection from natural disasters.

Many of the recommendations are interrelated. The implementation of the recommendations directly affecting agricultural producers, such as providing adequate coverage, are essential to the overall success of the Federal crop insurance program. At the same time, the recommendations that more directly address concerns of the insurance industry, such as providing for a more efficient structure for the FCIC, are also essential to the success of the program. The implementation of these recommendations will enable the two delivery systems to more efficiently deliver the insurance product to the Nation's agricultural producers. If producers are not pleased with the program, it is logical to assume that the insurance industry is also not pleased with the program. Conversely, if the insurance industry is experiencing difficulties in its attempts to provide insurance, it is likely to adversely affect agricultural producers. A healthy insurance industry is essential to the success of the Federal crop insurance program.

The Commission is committed to the development of a sound, consistent, reliable, and efficient Federal crop insurance program. If crop insurance is to be the risk management tool of agricultural producers in the future, there is a critical need to substantially improve the current program from the standpoint of the producers as well as the insurance industry. The recommendations contained in the Commission's reports should, if implemented, greatly enhance the program.

The recommendations contained in the Commission's principal report are for major policy changes in the crop insurance program with the underlying purpose of encouraging greater participation by farmers. Legislation would be required to effect many of the changes. However, some of the changes could be made administratively by the Secretary of Agriculture under existing law, and the Commission, in its principal report, urges the Secretary to make those changes, as well as the administrative changes the Commission recommended in its interim report, as expeditiously as possible. If the Secretary elects not to implement the recommendations, as the Administration's budget announcement indicated, the Commission urges the enactment of legislation to require the FCIC to carry out the Commission's recommendations.

The submission of the interim and principal reports to the congressional agriculture committees and the Secretary of Agriculture did not mark an end to the work of the Commission. Under the statute, the Commission is charged with the responsibility of continuing to monitor the Federal crop insurance program and reporting on a monthly basis, through December 31, 1990, to the congressional agriculture committees and the Secretary on (1) the extent to which the recommendations of the Commission have been implemented, and (2) the level of participation in the program by producers.

The Commission considers the continued monitoring and monthly reporting a very serious responsibility. In addition to meeting the statutory requirements, the Commission intends to use the monthly reporting process as a means of furnishing the congressional agriculture committees and the Secretary with any additional recommendations it may develop on ways to improve the program.

In that regard, at its September 1989, December 1989, and February 1990 meetings, the Commission developed additional recommendations to improve the operation of the program and to assist in retaining the participation gained during the 1989 crop year. A summary of the recommendations appears at the end of this statement as Attachment "D".

Mr. Chairman, this concludes our prepared statement. We will be pleased to answer questions.

ATTACHMENT "A"
(from Commission's
Interim Report:
April 1989)

SUMMARY OF RECOMMENDATIONS

The Commission believes that many changes to effect immediate administrative improvements in the program can be made under existing law by the Secretary of Agriculture and the Federal Crop Insurance Corporation. These changes would foster increased participation by farmers.

To maintain the increase in participation that is occurring in 1989, it is imperative that the Commission's recommendations be implemented by July 1, 1989, the beginning of the 1990 crop insurance sales year.

The Commission's findings and recommendations fall into four general categories: (1) increased responsiveness to producer needs; (2) broadening participation; (3) program simplification; and (4) improvement of delivery system performance. A summary of the Commission's recommendations follows:

1. Increased responsiveness to producer needs

-- Offer two alternative yield plans: general coverage based on ASCS yield and modified APH coverage based on the previous five years of data, but not less than the ASCS yield.

-- Standardize the unit definition within regions for commodity program crops and soybeans.

-- Establish peanut, cotton, rice, and tobacco units by share where there is a landlord/share tenant relationship.

-- Apply a premium rating policy to the entire farm, including division of units, and then permit a rate reduction for unit consolidation.

-- Permit farmers to exclude high risk land from their insured acreage.

-- Expand to other crops the futures market-based price election currently available for soybeans.

-- Explore the use of special endorsements that would allow a share tenant or a landlord to insure, in one policy, all interests in the crop.

-- Establish local committees composed of grower, industry, and FCIC representatives for each crop or group of similar crops to review new and existing programs.

2. **Broadening participation**

-- Develop a comprehensive education/training program for all participants in the Federal crop insurance program, as well as associated government services.

-- Implement a minimum commission payment or a flat payment as an incentive to expand the program in areas with small farms and low participation.

-- Develop financial incentives to compensate agents and companies for the special efforts needed to maximize participation in the undeveloped insurance markets.

3. **Program simplification**

-- Eliminate many problems associated with loss adjustment procedures by providing for: (1) expanded use of ASCS acreage certification, (2) "settlement on appraisal" agreements allowing final claim settlement based on mutually agreed upon appraisals, and (3) a special industry task force to determine alternative, less labor intensive methods of loss adjustment.

-- Synchronize all pertinent USDA commodity program and crop insurance dates to the maximum extent possible.

-- Allow producers who purchase crop insurance to use a simple certification statement for soil conservation compliance issues.

-- Limit the FCIC changes in policies, forms, rates, and procedures for the 1990 crop year to the changes identified in Commission reports.

-- Require that all Federal crop insurance information released by the FCIC (such as rates, rules, policy changes, and forms) be in place, for the entire upcoming crop year, by an early date.

-- Make automatic renewal of producer contracts at the same price selection option as in the previous year, even when the price within options changes.

-- Implement meaningful administrative tolerances for program determinations (including settling claims) to eliminate insignificant differences that are currently categorized as errors.

-- Initiate a review process for proposed rate, rule, and policy changes that carefully evaluates and analyzes the effect of such changes on producers, master marketers, and reinsured companies.

- -- Establish a joint FCIC-private industry committee to resolve, whenever possible, differences in procedures and policies.
- -- Establish an impartial review board for the settlement of disputes between FCIC and reinsured companies and master marketers arising from the handling of specific producer cases.

4. **Improvement of delivery system performance**

- -- Employ account executives to advise and assist master marketers and reinsured companies.
- -- Establish a periodic performance rating system for the operation of the reinsured companies and master marketers and the individual functions performed.
- -- Develop mutually agreed upon standards of performance for reinsured companies and master marketers.
- -- Develop financial incentives to encourage excellence in performance.
- -- Implement a system of monetary sanctions, and a system for referring cases to the Department of Justice for the imposition of civil and criminal penalties, for the false certification of information supplied to a company.

ATTACHMENT "B"
(from Commission's
Principal Report:
July 1989)

EXECUTIVE SUMMARY OF RECOMMENDATIONS

The recommendations in this report are for improvements in the Federal crop insurance program with the ultimate goal of providing to producers more equitable, efficient, and predictable protection from natural disasters.

The Commission's recommendations fall into four general categories: (1) increased responsiveness to producer needs; (2) broadening participation; (3) program simplification; and (4) improved program administration. A summary of the Commission's recommendations follows:

INCREASED RESPONSIVENESS TO PRODUCER NEEDS

Yield Guarantee Plans

- Offer the following voluntary yield plans: coverage based on the producer's Agricultural Stabilization and Conservation Service (ASCS) yield for ASCS program commodities and related commodities; coverage based on a county average yield for other commodities; and coverage based on a modified actual production history (APH) program yield for all commodities, and for ASCS program commodities, the APH yield cannot be lower than the producer's ASCS yield.
- Require the ASCS to establish soybean yields for crop insurance purposes.

Update ASCS Yields

- Require a revision of ASCS established yields, for crop insurance purposes, to accurately reflect actual production and to establish farm yields by practice.

Processor Yield Guarantee

- Establish guarantees for sugar beets and sugarcane that are based on the yield of the commodity after its initial processing.

Price Election Levels

- Enact legislation to authorize the Federal Crop Insurance Corporation (FCIC) to determine a maximum price election level based on one of the following methods, whichever is appropriate—(1) a futures market–based price election level, (2) a price election level based on the contract price of a commodity, (3) a projected market price at harvest time election level, and (4) a price election level based on the variable cost of production of the commodity. However, in no case may the maximum price election be less than the projected market price at harvest time. *
- Require the FCIC to announce the maximum price election level no later than 60 days prior to the sales closing date for insurance for the commodity and permit the producer to select any level up to the maximum level.
- Where appropriate, develop price elections that more accurately reflect the local price of commodities, and the differences in specific commodity varieties.

Prevented Planting

- Offer an effective prevented planting endorsement for excessive moisture.

Late Planting

- Review, and revise as necessary, all final planting dates and, in all policies for annual commodities, allow an automatic extension of up to 10 days, with a 1 percent per day decrease in the guarantee.

Experience Rating System

- Expand the experience rating system of premium discounts and surcharges that rewards or penalizes producers for their insurance experience.

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* NOTE: At its February 1990 meeting, the Commission agreed to substitute "total economic cost of production" for "variable cost of production" in clause (4).

Early Claims Adjustment

- Allow final claim adjustments, on crops yielding less than 20 percent of the program yield, to be based on the loss appraisal, thereby providing producers the option to harvest the remainder of the crop without a penalty.

Fire and Hail Exclusion

- Enact legislation to adjust the current limit on the amount of reductions in Federal crop insurance premiums when coverage for hail and fire losses is excluded from the policies so as to allow more actuarially sound and equitable reductions.

Unit Definition

- Standardize the unit definition within regions for ASCS program commodities and soybeans, apply a premium rating policy to the entire farm, including division of units, and then permit a rate reduction for unit consolidation.

Pilot Programs for New Methods of Insuring Against Agricultural Risks

- Enact legislation to specifically authorize the FCIC to conduct pilot programs to determine the feasibility of providing insurance coverage for agricultural risks through various methods not currently authorized under the Federal Crop Insurance Act.

County Loss Pilot Program

- Enact legislation that requires the FCIC to implement a pilot program to determine the feasibility of a Federal crop insurance program that bases indemnity payments on a county's loss of production, rather than on an individual's loss of production.

Pilot Program — 85 Percent Level of Coverage

- Enact legislation to require the FCIC to implement a pilot program for corn and a specialty crop under which producers would be permitted to purchase coverage equal to 85 percent of yields.

BROADENING PARTICIPATION

Level and Distribution of Premium Subsidies

- Enact legislation to provide for (1) a 30 percent premium subsidy for all coverage levels up to 75 percent of program yields, and (2) a temporary, additional premium subsidy for all coverage levels up to 65 percent of yields.

Eliminate Discriminatory Provisions in Other USDA Programs

- Ensure that no agricultural program, including disaster assistance programs, reduces or limits the benefits of the program due to a producer's receipt of Federal crop insurance indemnity payments.

Program Expansion

- Enact legislation to require the FCIC to offer insurance coverage for a commodity in all counties in a State if the FCIC offers such coverage in any county in the State.
- Expand the Federal crop insurance program to insure all commodities grown commercially in the United States.

Premium Rating System

- Establish premium rates on the basis of losses expected to occur in the future, using only the experience data that reflect normal risks, rather than relying on all losses that have occurred in the past.
- Review all county premium rates for each commodity and develop county rates on the basis of data on the county and the counties in the surrounding area.

PROGRAM SIMPLIFICATION

Improved Presentation of Coverage

- Change the presentation of the insurance guarantee to a dollar amount of coverage per acre.

Improved Presentation of Rate and Coverage Exceptions

- Clearly state in the policy all exceptions, requirements, restrictions, or other provisions concerning coverage and ensure that they are presented in a manner to permit the automation of the data using computer technology.

IMPROVED PROGRAM ADMINISTRATION

Cash Discounts

- Offer producers cash discounts for the early payment of premiums.

Develop Tracking and Individual Risk Underwriting Systems

- Enact legislation to authorize the FCIC to require participants to provide Social Security numbers, or individual tax identification numbers where appropriate, and develop a tracking system using such numbers to identify and monitor individual producers attempting to abuse the program.

- Expedite the development and implementation of an individual risk underwriting system to correct rating anomalies.

Penalty for False Certification by Farmers

- Enact legislation to provide for the imposition of civil penalties for producers who intentionally submit incorrect data or information.

- Develop language for all policies that could be used to assess liquidated damages against producers who intentionally submit incorrect data or information.

- Work with reinsured companies in developing language for inclusion in policies on the effect of producers intentionally supplying false information to a company.

Need for an Independent Appeals Process

- Enact legislation to require the establishment of an independent appeals system to review adverse determinations by the FCIC.

Improving the Administration of the FCIC

- Improve the efficiency of the program by, among other things, developing an improved and streamlined organizational structure for the FCIC; establishing a committee to advise the Board of Directors of the Corporation; using outside contracting to the greatest extent possible; and enacting legislation to establish, over the long-term, a new corporation to carry out the Federal crop insurance program.

Update Statute

- Enact legislation to update the Federal Crop Insurance Act by eliminating certain obsolete provisions and making the reinsurance program an integral part of the statutorily prescribed crop insurance program.

The Role of the FCIC as a Reinsurer

- Require the FCIC to reconsider the limitations the Corporation is placing on its role as a reinsurer of risks assumed by private crop insurance companies.

ATTACHMENT "C"

SUMMARY OF PROPOSAL FOR AN ALTERNATIVE PROGRAM

The alternative program would provide for two optional coverage plans. One would be based on area yields, and the other would be based on the producer's actual production history (APH). Under this program, there would be one price election level and one coverage level used to determine a maximum amount of dollars per acre in coverage. The price election level would be the current market price of the insured commodity 60 days prior to the crop insurance sales closing date for that commodity. The coverage level would be at 75 percent of approved yields.

Under the area plan, the maximum coverage would be determined by multiplying 75 percent of the county average yield for the commodity by the projected market value of the commodity. Under the APH program, the maximum coverage would be determined by multiplying 75 percent of the producer's APH yield by the projected market value of the commodity. If a producer has less than a 100 percent insurable interest in the commodity, the maximum would be adjusted accordingly. The producer would be given the opportunity to secure coverage of any dollar amount per acre up to the maximum.

For example, if a producer has a 100 percent interest in an insured crop of wheat and the projected price of wheat is $4.00 per bushel, the maximum coverage that a producer could choose would be --

(1) under the area plan in a county with an average ASCS wheat yield of 30 bushels per acre, $90.00 per acre ($4.00 per bushel times 75 percent of 30 bushels per acre); and

(2) under the APH plan where the producer's wheat yield is established at 40 bushels per acre, $120.00 per acre ($4.00 per bushel time 75 percent of 40 bushels per acre).

Under the area plan, yields would be based on the county average yield for the commodity; for ASCS program commodities, yields would be based on the average ASCS yield for the commodity in the county.

Yields under the APH plan would be determined on the basis of the producer's actual production records for the previous 5 years, using "Olympic averaging" (i.e., dropping the highest and lowest yields prior to averaging). In the case of ASCS program commodities, ASCS yields would be used for any year in which the producer does not have adequate production records.

The current method of determining crop insurance policy units would be used, providing basic units under the area plan and optional units for producers participating in the APH plan. There would not be a surcharge for optional units.

Losses would be adjusted on the basis of dollars per acre by multiplying the amount of coverage that the producer had chosen by the percentage the producer's actual yield was less than 75 percent of the county average yield, in the case of the area plan, or 75 percent of the producer's APH yield, in the case of the APH plan. Loss adjustment procedures would be developed by the National Crop Insurance Services (a private organization) and would be subject to approval by the Federal Crop Insurance Corporation (FCIC). Private companies and organizations would handle all loss adjustments.

The private companies and organizations would develop all the rules for marketing crop insurance policies, but the rules would be subject to approval by the FCIC. All crop insurance agents would receive training from private companies and organizations. The current "dual delivery system," reinsured companies marketing their own policies and master marketers marketing the policies written by the FCIC, would be retained.

Premium rates would be developed by private companies and organizations, subject to FCIC approval. The rates would be developed on a county-wide basis by commodity and farming practice. The rate would be quoted to producers on the basis of cost per $100.00 of coverage. There may be a need for (1) premium rate credits for producers who have a history of rarely incurring losses because they consistently produce high yields, and (2) premium surcharges for producers who have a history of excessive losses by not being able to produce yields equal to the county average.

Premium rates under this program would be established on an actuarially sound basis and would reflect all administrative expenses of the program (the FCIC's costs as well as the delivery systems' costs) and underwriting gains. The rates would also be weighted for catastrophic losses.

To make the premiums affordable to producers, increased government premium subsidies would be needed. Funds to offset this expense to the government would be available from (1) the elimination of the need for further disaster assistance programs, and (2) the reduction or elimination of the "unintended subsidy" that exists in the current program whenever indemnity payments exceed premium income. The establishment of actuarially sound rates would also allow the reinsured companies to assume a greater share of the risks of the program, thereby further reducing the costs to the government, and would permit the development of a reinsurance agreement for the reinsured companies based upon stop-loss coverage for which a premium could be charged by the Federal government. [Stop-loss coverage means that when losses incurred by a reinsured company reach a predetermined level, the reinsurer (in this case, the FCIC) would assume liability for losses above that level.] In addition, as producer participation in the program increases, the amount of the premium subsidy could be gradually reduced.

The primary focus of the FCIC would be the regulation of the program and providing reinsurance to the private companies. As such, the organization of the FCIC could be streamlined by restructuring the corporation to assure the effective and efficient administration of the program. There would be only four divisions within the FCIC, as follows: (1) Reinsurance; (2) Actuarial; (3) Compliance; and (4) Program Administration. The number of personnel and the government costs associated with administering the program would be greatly reduced because the role of private companies and organizations would be expanded. For example, private companies and organizations would be responsible for developing all new programs for commodities not previously insured under the program. The new programs would, however, be subject to approval by the FCIC.

ATTACHMENT "D"

SUBSEQUENT RECOMMENDATIONS

At meetings held subsequent to the issuance of the its principal report, the Commission adopted 9 additional recommendations to improve the Federal crop insurance program. A summary of these additional recommendations follows:

-- Provide for the ASCS county offices to transfer, electronically, established farm yields by farm serial numbers to the field underwriting offices of the FCIC, and for the field underwriting offices to incorporate this data, as a separate section, in their annual publication of actuarial information.

-- Work with representatives of the crop insurance industry, including representatives of the National Crop Insurance Services, to establish operational tolerances of at least 5 percent on acreages and yields and to allow for the revision of insured acreage and established yields, within such tolerances, to correct minor, inadvertent errors when discovered at loss adjustment time, whether or not coverage would be increased under the policy.

-- Review the problems in the crop insurance program for forage crops and make necessary corrections for the 1990 crop.

-- Expand the FCIC's futures market-based pricing concept, insofar as possible, and make adjustments in the methods for establishing the price election levels of specialty crops to more accurately reflect their price potential.

-- Standardize the method for computing price election levels to eliminate the potential for the arbitrary determination of such levels.

-- Enact legislation to authorize the issuance of injunctive relief or similar judicial processes against the FCIC or the Secretary to ensure that producers and companies are given the opportunity to seek prompt judicial review of adverse actions or decisions under the Federal crop Insurance program.

-- Consider using the total economic cost of production as a basis for determining the maximum price election levels in establishing price election levels under the program, in lieu of the variable cost of production that was previously recommended in the Commission's July 1989 report. (See page 1 of Attachment "B" of this statement.)

-- Take immediate steps to increase the highest price election level for grain sorghum under the 1990 program to reflect that commodity's traditional and well-established relationship with corn.

-- Consider developing a Federal crop insurance program based on sound insurance principles, giving special consideration to the alternative program included as Appendix B of the Commission's July 1989 report, a summary of which is set out in Attachment "C" of this statement.

Senator PRYOR. We are going now to our next panel. This is panel 5. This is the producer groups. We have Mr. Doyle Rahjes, president of the Kansas State Farm Bureau; AAM, the American Agriculture Movement, Mr. David Senter; and from the NFU, Tom Giessel, vice president of Kansas Farmers Union. We are very grateful for the three of you being here this afternoon.

I have seen Mr. Senter, and he has left the room momentarily. I think we have a very good replacement here, Mr. Corky Jones.

Mr. JONES. If that would be acceptable, Mr. Chairman.

Senator PRYOR. That would be fine, Corky. We appreciate you here.

Mr. JONES. Thank you.

Senator PRYOR. You have spent many hours sitting in this room, and we are glad that you are at our table this afternoon——

Mr. JONES. Thank you, sir.

Senator PRYOR [continuing]. Because those who are at the table we cannot just talk about the problems, we are obligated to help find a solution.

Doyle, we appreciate your being here. You are the president of the Kansas Farm Bureau Federation, and we appreciate your comments. Would you like to summarize your statement for the record?

STATEMENT OF DOYLE RAHJES, AMERICAN FARM BUREAU FEDERATION, PRESIDENT, KANSAS FARM BUREAU FEDERATION, AGRA, KS

INTRODUCTION

Mr. RAHJES. Mr. Chairman, I want to thank you very much for the opportunity to present Farm Bureau's position on crop insurance. As you have already indicated, my name is Doyle Rahjes. I am a wheat producer from Agra, Kansas. I have also been serving for the last year as Farm Bureau's representative on the Commission for the Improvement of the Federal Crop Insurance Program.

Farm Bureau has long been a supporter of crop insurance and continues to be supportive of the program today. That is not to say we believe the present program is working for all participants, but we firmly believe some type of a crop insurance program is preferable to a permanent disaster program.

CONCERNS ABOUT THE ADMINISTRATION'S PROPOSAL

We are very concerned about the administration's concepts put forth in the 1990 farm bill proposals. Many farmers are told the administration is supporting a disaster assistance bill, and they assume it is simply making permanent provisions similar to those in the 1988 or 1989 ad hoc disaster bills. Mr. Chairman, as you well know, the disaster concepts supported by the administration are a far cry from the 1988 or 1989 laws. Our concerns about their proposal include:

First, eligibility for the program is limited to crops currently covered by the FCIC as well as hay and forage. This means about 50 crops would be covered under the new program; however, under the 1988 disaster bill about 595 crops were covered. This means a lot of crops would not be eligible for disaster assistance under the administration's proposal and, presumably, crop insurance would not be available as an option either. With all the new experimental crops coming into production, limiting eligibility simply does not make sense.

Second, disaster payments would only be available in counties where actual county average harvested yield falls below 65 percent of normal. The question is what happens to the farmer who suffers a total crop loss on his farm, but happens not to live in a county which suffered only a 35 percent loss?

Third, once a county is declared a disaster, the individual producer would have to suffer a 40 percent loss of county average yield before he is eligible for aid. This simply does not make any sense to base aid on county yields rather than individual yields when production can vary greatly due to rainfall, cropping patterns, and so on. In order to suffer a loss below 60 percent of the county average yield, it could easily mean a good farmer would have to suffer from a 70 to 80 percent loss before they would qualify.

Fourth, payments are based on 65 percent of a 3-year average market price. That is much different than 65 percent of the target price, as was the case in the 1988 and 1989 disaster bills.

ONE OTHER MAJOR POINT

One other major point to keep in mind is that depending on how many years the administration proposes to use to come up with its average harvested yield could make a big difference in the coverage level. Most of the country had very low yields in 1988 and some parts suffered also in 1986, 1987, and 1989. Therefore, the average county harvested yield is likely to be lower than many farmers might anticipate, making it even more difficult to qualify.

With respect to crop insurance, we do not claim to have all the answers. We do, however, have some basic philosophies we are pursuing. Let me also assure you, Mr. Chairman, that our farmers readily admit that the major reason crop insurance is not working is because many producers believe disaster assistance will become available in time of need. We are willing to eliminate disaster assistance, but only when a crop insurance program is made workable and equitable.

IT IS ALSO EXTREMELY IMPORTANT THE CROP INSURANCE PROGRAM BE OVERHAULED

It is also extremely important the crop insurance program be overhauled. Additional band-aid approaches simply will not work. The program must be overhauled or the perception of the program will kill any future progress.

One of the most critical aspects of any crop insurance program is that it must cover program and nonprogram crops as well, cover them equitably. That is not to say that coverage must be identical, but it must be equitable. The equitability question works both ways. On one side of the coin, Farm Bureau is strongly opposed to linking crop insurance with farm program participation. Doing so may be the easiest and the least expensive way to increase participation, but it does not recognize the fact that some people do not need crop insurance. Certainly, it is a risk management tool, but it is not the only risk management tool. Because producers have ways of managing their own risk such as irrigation, diversification and self-insurance and do many other things to insure against a disaster. Forcing all individuals to take crop insurance is a serious mistake. The other side of the coin in equitability is that Farm Bureau will do everything possible to make sure that we do not try to solve the crop insurance problem only for farm program commodities while ignoring nonprogram crops.

We believe the program should be actuarially sound, developed by private industry and have catastrophic reinsurance and program administration provided by the Government.

The program should provide coverage based on dollars per acre. Each participant would be able to assess their liability and purchase the amount necessary to provide coverage needed. A deductible should be included to reduce premium cost and to stop nuisance claims. This would make the program simpler to administer and simpler to sell, thereby increasing participation.

I appreciate the opportunity to testify today Mr. Chairman, and would be happy to answer any questions.

Senator PRYOR. We are honored to have you here this afternoon, and I am going to next call on Mr. Corky Jones. Corky.

STATEMENT OF CORKY JONES, ON BEHALF OF THE AMERICAN AGRICULTURE MOVEMENT

Mr. JONES. Thank you, Senator. I apologize for David Senter's absence, but we have more places to cover this afternoon than we can possibly get covered.

Senator PRYOR. Right. We understand that.

INTRODUCTION

Mr. JONES. My name is Corky Jones. I am a farmer, the type of people that this entire committee has been talking about all day. I am not selling insurance. I am doing nothing but trying to make a living off of the farm.

Senator PRYOR. Corky, your home area is where?

Mr. JONES. My home area is southeast part of the State of Nebraska, another year of devastation as far as drought conditions. I have three sons in the family farm operation with me. I am here to represent them and myself and farmers and the American Agriculture Movement.

I am really definitely opposed to any attempt to abolish Federal crop. Some say Federal crop does not work. Senator, I can tell you that it worked for Corky Jones and his three sons. It worked for 174 other farmers in about a 30-mile circle from my home town. It is the difference between us being in existence and being on the auction block.

The auction block—let me mention just a little bit about that—we have a biweekly paper that comes out and just really deals with implement dealers and farm sales and public auctions. Two weeks ago this paper came out, and we have been really running a little slack of having the normal auctions during times of devastation, but 2 weeks ago in this same, about maybe, 50-mile circle, there was 51 farm auctions in that period. Now this is not all of them, but that is the ones they listed in this paper. This past week just before I came in the paper come out, there is 58. I have no idea whether that is any indicator of what the USDA's policies lead to, but I was also here just a few weeks ago when Clayton Yeutter made his proposal.

LOWER LOAN RATES, LOWER TARGETS, ABOLISHING THE FEDERAL CROP INSURANCE PROGRAM IS A BLUEPRINT FOR DISASTER

I am proud of Nebraskans. I am proud of being one. I am not proud of what the proposal from my fellow Nebraskan was. I can see with lower loan rates, lower targets and abolishing Federal crop insurance without a doubt that is a blueprint to not just the disaster and the erosion of farmers and ranchers from the land, but that is going to be erosion and a disaster for the very economy of this Nation. It is absolute disaster in any way you look at it. He said we are supposed to end up with higher net farm income. I ran through that through my paper computer and everything I have got and I fail to see how we could lower our prices for all we produce, do away with Federal crop and expect anything but substantially lower net farm income.

So we have got the work cut out for us. I heard mention representatives from the USDA, and he made a word there that kind of rang a bell for me. He said it is not privy. In my opinion, the privy that I would like to put in here, if all this happens and abolishing of farm programs is directed by our Secretary and the demise of Federal crop, we farmers across this Nation are going to be in a world of privy contents, the kind of privy I am talking about out on the farm. [Laughter.]

WE HAVE A PROBLEM: THE DEMISE OF THE FARMERS ACROSS THIS NATION

I am kind of mildly outspoken, but I am sincere, and I believe that we do have to be sincere, but we have a problem: the demise of the farmers across this Nation. Senator, when they talk about the total expense or whether USDA and the budget could possibly focus on this and meet that, we are not talking about what the claims that are paid to these farmers. We are not talking about any recognition at all about those dollars going back into the economy. Those dollars in Corky Jones' and sons' operation paid our lending institution, at least a portion of it. It paid those people that carried us for our fertilizer and our seed and our chemical. That is what happened.

So we cannot just say, well, it is a direct outlay. It did something about returning some investment and about doing something for the standard of living in this area. So we just cannot definitely just strike it off. I think we need to definitely salvage Federal crop. We need to improve it. In our written testimony that has been submitted here, which you are probably listening to me and looking at that, and nothing concurs at all, but you probably expected that when I sat down, too. [Laughter.]

TWO CONCERNS: PRICE AND FEDERAL CROP INSURANCE

I am a farmer, and I am taking an advantage probably of you by double whammying you, but I also do a lot of speaking and a lot of traveling across the Nation. I have traveled 17 States including every Senator that I have seen sit down here, and I have traveled those States. There is two concerns, two major concerns: we have got to have a price, not lowering the loan rates, not lowering net farm income or lowering the prices that we got, and we have definitely, the other thing is we have got to keep Federal crop insurance. That is the only fall back we have got. A visit to my banker just this past week said if we do not salvage Federal crop, we are going to see just literally dozens and dozens of our customers that we cannot even begin to make a production loan to, and that is including me.

Senator **Pryor**. Let me ask this, and we are going to move on to our next witness. Corky, as always, you speak from the heart. You mentioned your banker there, and that goes to the issue of credit. What does Federal crop insurance mean to a farmer's credit today? Now the USDA gentleman said it did not mean much so what does it mean?

Mr. **Jones**. He needs to go to the same house that I was talking about a bit ago. [Laughter.]

I can tell you that this Federal crop insurance means whether you are going to get a farm production loan or whether you are not. Ask the independent bankers in rural America all across this Nation, not just Nebraska, not just my area, but across the Nation. The 17 States that I have traveled I have seen this same thing happen. We believe, one thing that we believe that would surely help that possibly we should be looking at a signup in the farm program, a voucher for those farmers which in our area it is a big percent. I believe we have something like 83 percent of the farmers in my county that are using Federal crop, that buy Federal crop. We have a high signup, I believe in the low 90's, of farm program.

But it seemed like something that would work is a voucher paying the first 50 percent of that Federal crop for those people that join the farm program. I think it is something to look at.

Senator **Pryor**. Thank you very much, Corky. And we will place the statement of Mr. Senter of the American Agriculture Movement in the record at the appropriate place.

Mr. **Jones**. Thank you.

[The prepared statement of Mr. Senter follows:]

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TESTIMONY OF

DAVID SENTER, NATIONAL DIRECTOR

AMERICAN AGRICULTURE MOVEMENT, INC.

before the

Subcommittee on
Agricultural Production and Stabilization of Price
Senate Committee on Agriculture, Nutrition, and Forestry

March 6, 1990

I appreciate the opportunity to appear before this Committee to share with you my views concerning the problems with the Federal Crop Insurance Program. I am the National Director of the American Agriculture Movement, Inc. I appear here today as a representative of AAM, and the comments I will offer reflect AAM's position regarding the Federal Crop Insurance Program.

CURRENT PROGRAM INADEQUATE

What is most obvious is that the current Federal Crop Insurance Program is inadequate. Most farmers do not view it as a worthwhile program, and the majority do not participate. Therefore, the program fails to adequately protect farm income during droughts, floods, or other natural disasters or climatic conditions which significantly affect crop production.

This necessarily leads to one of two situations, neither of which is positive. First, when a significant crop disaster occurs, with broad regional or national effects, such as the droughts of 1988 and 1989, Congress has little choice but to step in with federal disaster relief measures. These are expensive, complex to design, and never totally effective at targeting those who most need and deserve the federal assistance. In addition, they require a broad political consensus, and with the budget limitations with which Congress must continually deal, this consensus will seldom be available.

Second, the current situation often leaves agricultural producers without any disaster relief. When the effects of the disaster are geographically narrow, or the numbers of farmers affected are small, federal relief is not usually available. For example, hail damage is often devastating, but it may affect only a few counties in a single state. In that situation, it is not possible to build the political consensus in Congress for a federal disaster assistance bill. Those farmers are left with little choice, except possibly to borrow more money to try to stay in business another year for another agricultural roll of the dice.

What is needed is a Federal Crop Insurance Program that will attract the large majority of producers, including at least all of those who participate in the federal crop support programs, and which will adequately protect them from major losses due to crop failures, making it unnecessary for Congress to step in with disaster relief measures.

FAIR PRICES ARE THE BEST FORM OF CROP INSURANCE

I should state at this point that the single most important step Congress could take to relieve this situation would be to enact a farm program that assures producers a fair price for their commodities -- at least the cost of production plus a fair return on the labor and investment. AAM has long called for parity pricing. If farmers were paid a fair price for their crops -- from the marketplace, rather than from a government check -- they could suffer through an occasional crop failure without the current dependency on a Congressional bailout. Were we able to make a fair profit most years, we could set a little aside to carry us through a bad crop year once every fourth or fifth year. But that is not the situation today.

The 1985 Farm Bill established a system for establishing progressively lower farm prices each year, lowering net farm income and driving many farmers out of business, regardless of the weather. Those of us who have managed to stay in business are mostly running marginal businesses; that is we barely make it, and we certainly cannot set anything aside to carry us through a bad crop year. With low farm prices, there is simply no ability to survive a disaster without a federal bailout.

NEEDED IMPROVEMENTS

Even with fair prices, there will be crop disasters of sufficient magnitude that a working system of federal crop insurance will be needed. Let me now briefly address myself to that.

PREMIUMS, COVERAGE, AND YIELD

Basically, the current system of crop insurance charges farmers too much for their premiums and pays them too little in coverage. That is the simple truth that accounts for the low enrollment in the program. Any meaningful improvements to the current program will have to address both of these problems. The ratio of premium to coverage must be greatly improved.

Today farmers are required to absorb too much of the loss before crop coverage kicks in, and the yields are established too low. In particular, even under the highest coverage, the farmer must absorb from 25 - 50% of the loss before the insurance coverage applies.

In determining yield, the ASCS projected yield is the usual starting point, reduced by a "T-Factor" which ranges from approximately 15% to 30%. Coverage, for example, that claims to be 50% coverage, in fact protects considerably less than 50% of the actual yield.

For example: A farmer with an ASCS projected yield of 680 lb./acre of cotton, insures it for the maximum coverage of 75% at the maximum rate of 55¢/lb. and the coverage would be $207.48 with a premium of $22.40.

If a farmer is fortunate enough to have his 10 year records, the "T-Factor" will be dropped, and then the same 680 lb. yield would cost him $14.02 for $280 worth of coverage. I would like to point out that according to Mississippi State University the cost of production for 680 lbs. of cotton is $517 per acre.

It can be seen by these figures that a farmer can take the maximum coverage, have a short crop, go bankrupt, and never collect one penny in insurance. Why insure a loss?

To correct this, the T-Factors should be eliminated, and the yield should be determined as nearly as possible on actual yield. Three to five years should be adequate to prove actual yield, and any year reflecting a major crop failure should be eliminated from the average. Whenever the ASCS projected yield is necessary, it should not be reduced by a T-Factor. Also, the maximum coverage should be close to the total cost of production.

Also, the current program has the government paying 30% of the cost of 50% and 65% coverage, but only 19% - 20% of 75% coverage. This misdirects most farmers who enroll in the program to elect lower coverage and assures lower protection. To minimize risk and cash flow disruptions, the government should offer an incentive for the higher coverage, by paying at least the same percentage, and perhaps a higher percentage of those premiums.

PROGRAM ABUSES

There are other problems with crop insurance today that pertain to that small percentage of the farmers who try to cheat the system. Most farmers are honest and their claims are legitimate. Unfortunately, there are a few folks out there who successfully abuse the program. The added ~~costs~~ of these abuses, though practiced by only a small percentage of farmers, is partially borne in higher premiums by the vast majority of honest farmers. Requiring better verification of loss claims by County ASCS Officials, if possible, would reduce this problem.

LOW RISK AREAS SUBSIDIZE HIGH RISK AREAS

Another problem seems to be that the cost of crop insurance is determined by an average of costs which includes both high and low risk areas. Those of us who farm in a low risk area, end up paying more than we should for coverage to reduce the cost in high risk areas. This cost averaging system works as a disincentive for farmers from low risk areas to enroll in the program.

GOVERNMENT SHOULD PROVIDE MINIMUM COVERAGE

I realize that this Committee is charged not simply with identifying the problems in the current program, but also with enacting what changes need to be incorporated in the program to assure that it accomplishes its primary goals in the future. I have some suggestions I would like to offer.

First, all producers who participate in federal farm programs should be provided automatically, and at no cost, basic minimum crop insurance coverage of at least 50% of their actual proven average yield. We realize the budget impact of this proposal, but this is the price government must pay for the cheap food policy which has forced us into the position of producing at substandard prices. Congress ends up having to come in and spend enormous sums of money to reimburse producers following a disaster now. It would be better for the Congress to spread the cost over several years by providing this basic coverage to all who participate in the federal programs. This would greatly increase the numbers of farmers in the program, and the cost to the government per farmer would be greatly reduced.

At the time of sign up for the federal farm program, the producer would receive a voucher from ASCS which would entitle him to 50% coverage at no cost. The program should be a government self-insurance plan through the ASCS office.

Obviously, 50% coverage, even based on actual yield, would not be sufficient to adequately protect most farmers against a dramatic loss of revenue. Therefore, farmers should be provided the option of purchasing additional coverage, up to 100% of their actual yield, at their own expense from private insurers. This additional coverage would not be cheap, but if farmers are paid a fair price for their crops, and if the coverage provides real protection against a crop loss, most farmers could afford to pay the premium for the extra coverage to limit their financial risk. This program would bring a stability to farming that is badly needed.

SUMMARY

Farming will always involve a degree of uncertainty and risk. Farmers are accustomed to that, and are willing to take reasonable risks. Crop insurance should be designed to remove unreasonable risks -- those over which the farmer has no control and which can destroy a farming operation, despite hard work, good planning, and sound management.

The basic coverage (50%) -- that which protects a producer from a disaster which can destroy a lifetime of work in a single season -- should be provided at no cost to those who participate in the federal farm programs. Congress can accomplish this by spending a modest amount on crop insurance each year, instead of billions at one time in a Disaster Relief Bill, plus, it would be an incentive for program participation.

Additional coverage should remain an option for the individual farmer to consider each year. Should he decide to assume the risk, he can save the cost of the premium; should he decide it is more important for him to avoid the risk, he can elect to incur the expense of the additional coverage. That would be a business decision within the discretion of each individual producer.

When Congress fails to maintain adequate loan rates and target prices, they must instead have a complex system of gimmicks in order to prevent wide spread bankruptcies and foreclosures in an attempt to keep farmers on the land. Federal crop insurance of the past has been one of those gimmicks.

Senator **Pryor**. Now we will go to Tom Giessel. We appreciate you being here.

STATEMENT OF TOM GIESSEL, NATIONAL FARMERS UNION, VICE PRESIDENT, KANSAS FARMERS UNION, WASHINGTON, DC

Mr. **Giessel**. Thank you, Mr. Chairman.

INTRODUCTION

As you know, I am Tom Giessel from Kansas. I am representing the National Farmers Union, some 300,000 family farmers, and we are right at this time holding our national convention, and I brought with us a Special Order of Business [9] concerning crop insurance from our convention which I wish to be part of the record, and basically, in short, it says we support the program and we think it is imperative that we act quickly and expeditiously to continue and improve the program.

I farm in western Kansas with my brother where we have about 3,800 acres on which we grow wheat, grain sorghum, milo, and alfalfa, using both irrigated and dry land. We are fairly diversified, and we participated and believe in the crop insurance program, and we have for many years. We are a strong proponent. I also serve as a member of the Commission for the Improvement of the Federal Crop Insurance Program.

WE HAVE SEVERAL PROPOSALS WE FEEL THAT WOULD HELP TO IMPROVE THE CROP INSURANCE PROGRAM

We have several proposals we feel that would help to improve the crop insurance program. Three basic areas that I think are the heart of it are the price election; yield options; and coverage.

PRICE ELECTION SIDE

On the price election side, we believe strongly in a price election based on cost of production or total economic cost. It would provide stability to the program.

You have seen in the last few months announcements made on price selections that jump back and forth and all over, and farmers cannot plan with this type of movement in the variables within the program.

YIELD OPTIONS

Yield options, we believe in the APH, but we also believe there has to be some floor or bottom, much as some of my friends from the Crop Insurance Commission have recommended.

COVERAGE

The coverage currently, of course, is 50, 65 and 75 percent, and we believe it should be raised to 60, 70 and 80 percent. With these improvements, a producer would be allowed to use any combination to fit the program, I believe, to his or her needs.

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[9] See p. 130 for the Special Order of Business.

EVERYBODY TALKS ABOUT THE PRICE AND YIELD

On our field hearings and the Commission, plus everyone I have talked to out in the country, be it a lender or farmer, whatever, everybody talks about the price and yield. And those are the two important factors.

PREMIUM SUBSIDY

We also believe that the premium subsidy should continue, and it should be consistent through all three levels of coverage meaning that on the top level we would like to see that increased to 30 percent. That way farmers will not be more or less directed to the middle level of coverage.

We also believe that we could see better coordination between ASCS and FCIC with like the 1026 and 476 acreage reports to where we could simplify that. I think with the computers that our county ASCS offices have we could simplify that and save a lot of hassle.

DISASTER POOL

Earlier today it was mentioned about disaster pools, and we believe in that concept also, having a disaster pool maybe funded from savings in deficiency payments to be above and beyond in the event of catastrophic events.

THE POTENTIAL EFFECT OF SHUTTING DOWN CROP INSURANCE

The potential effect of shutting down crop insurance is, I think, should send shock waves through rural America. The administration's proposal for a disaster program has also been not well received. I fear personally that if we shut down the FCIC that many private insurance companies will not be willing to come into areas like mine in the Plains States and write insurance, and where is that going to leave me? And couple that with the disaster proposal, I would have a lot of trouble, I think, going to a bank and when I go through and fill out my financial statement, if I listed disaster program, that would not carry much weight at all. Now crop insurance does carry some weight.

In fact, a local bank board member told me before I came in that if crop insurance was eliminated, he said they would have to go through and start drawing lines through people's names, and it may not be them. It might be bank examiners who step in. They may not even have the choice. So I think we would eliminate a good number of family farmers by this action.

The disaster program proposed by the administration just does not offer adequate coverage. The 40 percent deductible in order for you to get coverages is very unrealistic. I suppose I insure my house for fire. I would not think of 40 percent of houses in the county would have to burn down before I could collect. I do not see why we should have to have a program like that for crop insurance.

UNTIL WE HAVE CROP INSURANCE FIXED OR DO NOT HAVE CROP INSURANCE THAT WE SHOULD HAVE A CROP ASSURANCE TYPE OF DISASTER PROGRAM

We believe that until we have crop insurance fixed or do not have crop insurance that we should have a crop assurance type of disaster program, and basically would be available to all producers, cover all crops, based on dollars per acre and would cover economic cost of production, not the profit, but the economic cost of production. This is not our choice, but we cannot be left bare out in the country. This is not only a producer issue. Crop insurance is a rural economic issue.

CONCLUSION

I might just add that I think, as a final note, there has been a lot of damage in the countryside by the announcement of the possibility of shutting down crop insurance. I rent land from a lot of retired people, and I went over about a month ago and visited with one of my land ladies and went on through the visit. And pretty soon she said, well, she said I guess I will not have crop insurance next year. And I just had her signed up. I worked to sign her up a year ago.

And she said, well, they said on television we are not going to have it. So how many hundreds of people are out in the country confused by this announcement? So I think it has dealt a severe blow, but the bottom line is crop insurance is just too important to eliminate. That concludes my remarks.

Senator PRYOR. I want to thank you very much. Those were splendid statements.

[The prepared statement and Special Order of Business of Mr. Giessel follow:]

NATIONAL
FARMERS
UNION

TESTIMONY OF THE NATIONAL FARMERS UNION

Presented by Tom Giessel
Vice President, Kansas Farmers Union

before the
Senate Agriculture Subcommittee for
Agricultural Production and Stabilization of Prices

March 6, 1990

Testimony of Tom Giessel, Vice President of Kansas Farmers Union, presented to the Senate Agriculture Subcommittee for Agricultural Production and Stabilization of Prices, on March 6, 1990.

Good afternoon. I am Tom Giessel. It is a pleasure to appear here today on behalf of the National Farmers Union and as Vice President of the Kansas Farmers Union. The National Farmers Union is a general purpose farm organization with approximately 300,000 farm family members.

I am involved with crop insurance as a farmer and a member of the Commission for the Improvement of Crop Insurance, which was established by Congress. I farm in partnership with my brother in Kansas, where we have about 3,800 acres on which we grow wheat, grain sorghum, and alfalfa, using both irrigated and dry land. Our farm has always used crop insurance and I would like to see the crop insurance program continue.

There are some areas of crop insurance that can and should be improved and I appreciate the opportunity to discuss these suggestions with you today.

If crop insurance is to provide an effective risk management tool and obviate the need for major ad hoc disaster assistance programs, then we must increase producer participation. The three leading proposals to accomplish this goal are: 1) making the coverage mandatory, 2) offering the coverage for free, or 3) improving the product to make crop insurance more attractive to producers.

We believe crop insurance does not need to be mandatory or free, as long as it makes good business sense. The biggest drawback under the present program is that many producers are unable to cover their costs of production, even if they select the highest price elections and yield options offered. Producers around the country testified time and again during commission hearings that the most important improvement was to increase the price and yield options to allow a producer to cover a larger portion of his total economic costs.

National Farmers Union supports increasing the current yield options of 50, 65, and 75 percent to levels of 60, 70, and 80 percent. The price options should be increased so that at a minimum the producer can recover his variable costs, with a higher option to allow the producer to recover income from the crop.

The second improvement we recommend is to offer the same percentage of premium subsidy for each level of coverage. The current choices offer a lower percentage of premium subsidy to producers who select the highest level of coverage. If the goal is to eliminate the need for disaster payments, then the crop insurance program should encourage producers to select more coverage rather than less.

We would like to see premium subsidies targeted to family size farms.

Crop insurance could also be improved by basing coverage on the farmers actual production history (APH). Using a county average unfairly discriminates against the most efficient producers, thereby discouraging their participation in the program. An added advantage of using APH is that it would discourage moral hazard.

Coverage for new farmers could be based on county averages until production history was available for their farms.

Sign-up for crop insurance could be simplified by a better co-ordination of administrative functions such as acreage certifications and conservation compliance between ASCS and FCIC. Then farmers could be given a letter of compliance at the time of their ASCS certification to be used in lieu of recertifying for FCIC.

We would also like to see savings from deficiency payments used to create a disaster pool. This money would then be used to provide additional assistance to insured farmers in years of disaster. This money would be unavailable to be used for non-insured producers, but once the crop insurance program is fixed, farmers could be responsible for their own risk management.

If the above-stated modifications were implemented, we believe participation would be substantially increased. The addition of low-risk producers should assist in achieving the goal of reducing the present premium to loss ratio, which is estimated at 1.5.

The administration has proposed eliminating crop insurance and implementing a disaster program. While some assistance programs may provide a viable alternative to crop insurance, the administration's program would be likely to ensure a disaster rather than prevent one.

The administration's program leaves farmers who suffer a disaster with no recourse unless the rest of their county has the same disaster. Even then, the producer's ability to recover is limited by the 40 per cent deductible built into the administration's proposal. Worse yet, the producer is unlikely to even have the opportunity to purchase private crop insurance because insurance companies have stated that they would be unwilling to provide coverage if the government were not providing re-insurance.

Another unfortunate and perhaps unintended consequence of the administration's proposal is that it could operate to deny protection to a producer who exceeds the county average for production and suffers a loss, while subsidizing the producer with below average production.

If Congress were to adopt a disaster assistance program in lieu of crop insurance, it should operate as a revenue assurance program. Coverage could be provided to program participants as an incentive to participate in commodity programs. Coverage could also be extended to non-program crops. The level of coverage should be based on the total economic cost of production per acre, including fixed and variable costs, but excluding opportunity cost. Yield history would be based on actual production history or regional yields.

The program would be administered through county ASCS offices. In the case of disaster, the producer would have his land certified by the ASCS office to receive an advance at harvest time. Any money he received from marketing his crop would be required to be paid back against his advance, thereby insuring the producer a certain level of income for each crop planted.

The producer would still be better off with a normal crop than the revenue assurance payment, but revenue assurance would help the producer meet expenses in the case of a disaster. It would also provide the security many banks demand before making loans.

Adequate risk protection will never be cheap, but in assessing the appropriate level of funding, Congress should remember that a weather disaster affects more than just the producers who lose their crops. In 1989, my home county, Pawnee County, Kansas, should have harvested a wheat crop worth $16 million, based on the number of acres planted, the normal yield for the county, and using a price of $4.00 per bushel. Instead, producers from my county received $1.6 million. Disaster assistance replaced only $4.5 million of the lost income. As one would expect, everyone in the community suffered from the loss of almost $10 million, and the effects will be felt for some time to come.

During the past two years, the Commission for the Improvement of Crop Insurance has listened to many farmers testify and has discussed many proposals in an attempt to come up with the ideas which will "fix" crop insurance. While we did not always agree on every issue, we do believe that with the right changes crop insurance can and will provide the stability necessary to ensure a steady food supply and to prevent rural communities from being devastated. Thank you for this opportunity to share our views.

NATIONAL
FARMERS
UNION

SPECIAL ORDER OF BUSINESS
Adopted by Delegates to
the 88th Annual Convention
National Farmers Union
Oklahoma City, Oklahoma

March 4-7, 1990
FEDERAL CROP INSURANCE PROGRAM

Whereas National Farmers Union supports the Federal crop insurance program; and

Whereas crop insurance is a necessary risk management tool in many family farm operations;

Whereas farmers in some parts of the country are facing drought conditions for the third year in a row; and

Whereas government support is necessary for the continued availability of crop insurance; and

Whereas members of Congress are currently assessing options for the improvement of crop insurance; and

Whereas the administration has eliminated funding for crop insurance in the proposed federal budget;

We recommend that all members of the National Farmers Union urge their members of Congress and the president to continue and improve the federal crop insurance program.

Senator **Pryor**. Senator Kerrey. Senator Kerrey, by the way, I have been informed that shortly after 5, probably about after 10 after 5, we will have a vote on the Senate floor on the Baucus amendment to the clean air bill. So we have one more panel, but I think we have adequate time should you want to pursue any questions.

Senator **Kerrey**. I really have no questions other than to thank the panel and to inform them that we will be developing legislation to try to correct some of the problems that we see in the crop insurance program and to put in place a program that serves farmers better and that is fully accountable to the taxpayers as well. I urge you to follow the development of the legislation because the detailed input that you could give us would be very valuable. So thank you again for appearing.

Mr. **Giessel**. Thank you for the opportunity.

Senator **Pryor**. We appreciate very much the three of you being here this afternoon. You have made a great contribution to this hearing, and we will now call our final panel.

Mr. Max Claybaker, a wheat farmer and insurance agent from Blackwell, Oklahoma; Mr. Richard Gibson, chairman, American Association of Crop Insurers from Council Bluffs, Iowa; and certainly last but not least, Mr. Bill Bracey, National Association of Professional Insurance Agents and Bracey Insurance Agency, from Blytheville, Arkansas.

Max.

STATEMENT OF MAX J. CLAYBAKER, WHEAT FARMER, INSURANCE AGENT, BLACKWELL, OK

Mr. **Claybaker**. Senator Pryor, Senator Kerrey, I thank you very much for letting me come here and talk to you. I will, with your permission, I will not read any of my testimony. You have copies of it, I presume.

Senator **Pryor**. You may summarize. We are going to place the full body of your testimony in the record. If you would just tell Senator Kerrey and myself what you think is wrong and what we need to do to correct the program.

INTRODUCTION

Mr. **Claybaker**. Mostly what I want to do is tell you what I think is right.

I want to emphasize with you gentlemen that I am a third generation farmer. I have my youngest son, who is a student at Oklahoma State University, and he will follow me in about 2 years. We farm on purpose. We farm about 1,500 acres of wheat in north-central Oklahoma and about 4 years ago with the idea that possibly my youngest son might take over the farming operation.

MAYBE WHAT IS IMPORTANT IS I WEAR BOTH HATS

My son-in-law said why do you not maybe sell crop insurance. He had a P&C agency, and he says I hate this stuff. So I got a license and I got started. And I think what I want to say here, maybe what is important is I wear both hats. I am a genuine farmer, and I try very, very hard to take care of my farmer insureds, and Senators, I was up at 4 o'clock in the morning this summer—I will look you both in the eye and tell you that—many mornings till the phone would not ring to take care of my farmer insureds. And I do not think FCIC people do this. Nobody sent me out here. I paid my own plane ticket and I paid my own motel. Just my money that I came out here, but I am concerned about losing this program.

DISASTER VERSUS INSURANCE

And my farmers are scared. We talked about disaster versus insurance, and I realize what we are getting down to here, the bottom line is are we going to have a disaster program or are we going to have crop insurance. I paid many farmers this year bona fide crop insurance claims. They did not cheat. It makes me very angry to hear this cheating thing. I am over 21, quite a few years, and I know this happened years ago. But my companies, and I represent three private companies, and they are telling me you had better do your paperwork and do it right, and I do have it right. One company thinks I have the best file in the State of Oklahoma. I welcome your audit any day.

CLAIMS

So we are really concerned about this, and many of the farmers who collected crop insurance payments from me did not collect a penny of disaster payments, and you are looking at one for the simple reason I had two farms under one farm serial number. They were opposite ends of the county. And I like to think of crop insurance as mini-disasters, M-I-N-I, not M-A-N-Y, but mini-disasters. The vast majority of the claims I paid are these: where farmers have cheat infested fields. You can be the best farmer in the world and have a late freeze, and that has happened in parts of my county. In other parts it did not.

I had a 51-bushel wheat crop average on my half section where I live this year, and Senator Pryor, 5 miles west of my house, Senator Kerrey, those people out there, the best farmers in Kay County, got 5 bushel, 10 bushel, 15 bushel of wheat. We got 6 inches of rain from Hurricane Gilbert, and they got 2, and that was the difference, pure and simple.

One thing that scares me, I hate to go the ASCS office. And we have a very fine one, good people, but you are there all day. If we end up getting this program back in the ASCS office again, we are going to have everybody in there with their crop insurance, and in the meantime I and many other fine crop insurance agents could take care of their problem and get them home quicker.

INSURANCE

So I will go on and get off that. I moved my own policy up this year from level two to level three. You know why? I am like you. I hate insurance. But I asked a farmer one time, he complained I never collect anything on my crop insurance. I said you have got a good pick-up out there. You got liability? He said yeah. I said do you want to kill somebody to see if you are going to collect or not? So he kind of thought that over, you see. And yes, I hate to pay the insurance and I just spent about $7,500, but I tell you what, about

4 weeks ago I was awful glad I had it. We have had rain now, and I feel much better.

Not one thing has been said here today, gentlemen, about people buying this stuff. We keep talking about money going out, money going out. Mr. Marshall was here awhile ago. I asked somebody who is that man. He said Mr. Marshall, and I recognized him then. And 800,000 farmers paid into it. So it is not a total loss. It is a negative result from the standpoint of not quite getting back what you put in, but 800,000 farmers paid into it. And lastly, that red light is on, and I appreciate it. I got to catch a plane, too. I am nervous as heck about that.

CONCLUSION

I testified before this committee in Salina, Kansas last year on how to improve it, and it just dismayed me and frustrates me that all that work went into that, the work on my part, and nobody wants to take a look at it. And I am going to close those remarks. If you have questions, I will be glad to answer them. Thank you both very much.

Senator **PRYOR**. We are real proud that you came today and thank you for sharing your thoughts with the subcommittee.

[The prepared statement of Mr. Claybaker follows:]

CROP INSURANCE HEARINGS

WASHINGTON D.C.
6 March 1990

SENATORS-HONORED GUESTS:

MY NAME IS MAX CLAYBAKER. I AM A WHEAT FARMER FROM BLACKWELL, OKLAHOMA. MY YOUNGEST SON AND I PRODUCE APPROXIMATELY 1500 ACRES OF WHEAT. I AM HERE TODAY BECAUSE I AM CONCERNED THAT I WILL NOT BE ALLOWED TO PURCHASE CROP INSURANCE FOR MY WHEAT PRODUCTION AFTER THIS YEAR'S HARVEST IS COMPLETED. THIS PAST YEAR, I SUFFERED LOSSES ON TWO FARMS. CROP INSURANCE PAID BOTH LOSSES. WHEN I WENT TO THE ASCS OFFICE TO COLLECT MY DISASTER PAYMENTS WHICH HAD BEEN AUTHORIZED LATE IN THE SUMMER, I WAS DENIED PAYMENTS. BOTH FARMS WHICH HAD LOSSES WERE CONNECTED TO OTHER FARMS UNDER THE SAME FARM SERIAL NUMBER. THE OTHER FARMS PRODUCED QUITE WELL. THEREFORE, SINCE THE AVERAGE OF THOSE FARMS UNDER THE SAME FARM SERIAL NUMBER HAD PRODUCTION LEVELS ABOVE THE DISASTER THRESHOLDS FOR THOSE FARMS, I WAS DENIED PAYMENTS. IF I HAD NOT HAD CROP INSURANCE, THE OTHER FARMS WOULD SIMPLY HAVE HAD LOSSES, AND THAT WOULD HAVE BEEN THE END OF IT.

I HAVE BEEN FARMING SINCE 1956. I AM A THIRD GENERATION FARMER. ONE OF THE PRIMARY REASONS I CHOSE FARMING AS A CAREER WAS I HAD SEEN MY FATHER SUCCEED VERY WELL IN THE BUSINESS FOLLOWING THE CLOSE OF WORLD WAR II. I FELT VERY CONFIDENT THAT I COULD RAISE AND EDUCATE A FAMILY BY GOING INTO AGRICULTURE AS MY FATHER DID...AND HIS FATHER BEFORE HIM. IN 1982, MY APPRAISALS AND CONCLUSIONS DRAWN IN 1956 DIMINISHED CONSIDERABLY AS AGRICULTURE WENT INTO A DEPRESSION.

IN TODAY'S AGRICULTURE, RISK IS A COMMODITY I ABSOLUTELY CANNOT AFFORD. PRODUCTION COSTS ALWAYS COMPRISE THE MAJORITY OF THE INGREDIENTS FOR NEXT YEAR'S CROP. MY BANKER EXPECTS ME TO MAKE MY PAYMENTS ON TIME. MY SUPPLIERS EXPECT ME TO PAY THEM FOR THEIR PRODUCTS AND SERVICES I PURCHASE...AND WELL THEY SHOULD.

DISASTER PROGRAMS ARE HAZY, UNPREDICTABLE, COMPLICATED, AND POLITICALLY EXPEDIENT. THEY PROVIDE NO FOUNDATION FOR STABILITY....IN OTHER WORDS, "YOU CAN'T TAKE 'EM TO THE BANK"!

MY CROP INSURANCE POLICY TELLS ME EXACTLY HOW MANY DOLLARS I CAN EXPECT TO RECEIVE THROUGH LOSSES THAT MIGHT OCCUR. FURTHERMORE, I PERSONALLY HAVE CHOICES AND CONTROL AS TO HOW MUCH OR HOW LITTLE I WANT TO BUY TO COVER POTENTIAL LOSSES. I KNOW EXACTLY WHERE I STAND. THERE IS NO GUESSWORK OR QUESTION ABOUT WHAT'S GOING TO HAPPEN ~~VIA~~ VS DISASTER PROGRAMS...IF THEY ARE AUTHORIZED. THE BEST PART IS THAT I BUY IT BEFORE I PLANT THE CROP. DISASTER PROGRAMS ARE AFTER THE FACT.

I WOULD BE GREATLY DISTURBED IF IN MY PART OF THE COUNTY, YIELDS WERE LOW DUE TO LATE FREEZE, ISOLATED DROUTH(AS WAS THE CASE THIS PAST SUMMER)OR OTHER CAUSES WHILE THEY WERE EXCELLENT IN OTHER PARTS OF THE COUNTY. UNDER THE PROVISIONS OF THE PROPOSED DISASTER PROGRAM FOR THE NEW FARM BILL, THE COUNTY WOULD HAVE TO SUFFER MASSIVE COUNTY WIDE DISASTERS BEFORE ANY RELIEF WOULD BE ACTIVATED. THE FACT REMAINS,WITH THE ABOVE CONDITIONS, I WOULD NOT BE ABLE TO MEET MY COMMITTMENTS, WOULD BE UNABLE TO MAKE MY BANK PAYMENTS, AND WOULD HAVE TO BORROW AGAIN FOR NEXT YEAR'S CROP...A SEVERE SETBACK TAKING YEARS TO RECOVER.

I AM ALSO CONCERNED ABOUT ANOTHER "BIG" PROGRAM BEING IN THE HANDS OF THE LOCAL ASCS OFFICE. MY"DOWN TIME" AS A FARMER HAS INCREASED DRAMATICALLY BECAUSE OF DELAYS AND TIME SPENT IN THE ASCS OFFICE WAITING MY TURN TO PROCESS VARIOUS PROGRAMS. MY LOCAL ASCS OFFICE DOES A VERY COMMENDABLE JOB PROCESSING AND ADMINISTERING THE PROGRAMS THEY HAVE. THEY ARE OVERWORKED NOW AND WOULD REQUIRE THE EMPLOYMENT OF NEW EMPLOYEES TO ADMINISTER THE PROPOSED DISASTER PROGRAM.

FORTUNATELY OR UNFORTUNATELY, AS THE CASE MAY BE, MANY FARMERS TODAY HAVE "OFF-FARM" INCOMES. I FIND IT FRUSTRATING ON THE ONE HAND WHERE I AS A FARMER SPEND IN EXCESS OF 135000 DOLLARS EACH YEAR IN PRODUCTION COSTS TO PUT OUT NEXT YEAR'S CROP, NOT WITHSTANDING DECPRECIATION OF FARM EQUIPMENT, AND STILL FIND IT NECESSARY TO FIND OUTSIDE EMPLOYMENT TO BOLSTER MY INCOME FOR FAMILY LIVING, RETIREMENT, AND OLD AGE. ON THE OTHER HAND, I AM FORTUNATE IN HAVING "OFF-FARM" INCOME IN THE FORM OF AN AGENCY WHICH WRITES CROP INSURANCE FOR MY FARMER FRIENDS AND NEIGHBORS.

I TAKE THE JOB AND CHALLENGE OF WRITING CROP INSURANCE SERIOUSLY. I NOW WRITE COVERAGE FOR FARMERS IN 19 COUNTIES IN OKLAHOMA AND SOUTH-CENTRAL KANSAS. I HAVE AN OFFICE STAFF TO ASSIST ME. WE DO A VERY THOROUGH JOB OF TAKING CARE OF OUR FARMER INSUREDS. AS A CROP AGENT, I AM IN A UNIQUE POSITION OF BEING ABLE TO SEE BOTH SIDES OF CROP INSURANCE, NAMELY BUYING IT AS A FARMER AND WRITING IT AS AN AGENT. WE PRESENTLY HAVE CONTRACTS WITH THREE MULTI-PERIL COMPANIES. THIS PAST SUMMER, WE PAID OUT OF OUR OFFICE ALONE OVER 618000 DOLLARS TO FARMERS. THE UNIQUENESS OF THIS WHOLE AFFAIR IS THIS: IN THE PAST FOUR YEARS OF PROCESSING CLAIMS, THE VAST PERCENTAGE OF CLAIMS PAID OUT WERE TO FARMERS WHO SUFFERED "MINI-DISASTERS",...THAT IS, LOSSES INCURRED WHICH DRAMATICALLY AFFECTED THE JOB SECURITY AND PERPETUATION OF THAT FARMER, WHILE NOT BEING COUNTY WIDE OR EVEN FELT BY NEIGHBORS DOWN THE ROAD OR NEARBY. AGAIN, UNDER THE COUNTY DISASTER PROPOSED PLAN, THEY WOULD HAVE RECEIVED NO COMPENSATION FOR LOSSES. CROP INSURANCE LITERALLY KEPT THEM IN BUSINESS.

PARTICIPATION IN THE PROGRAM HAS BEEN ONE OF THE CRITICISMS OF CROP INSURANCE ADVERSARIES...THAT IS, THEIR CLAIM TO LOW PARTICIPATION. AND YET, THE GROWTH IN THE PAST TWO YEARS HAS BEEN PHENOMENAL. THE OPPONENTS CREDIT THE GROWTH OF COMPULSORY ENROLLMENT IN CROP INSURANCE TO THE RECEIVING OF DISASTER BENEFITS AS THE REASON FOR THE GROWTH IN PARTICIPATION. SUCH IS NOT THE CASE IN NORTH CENTRAL OKLAHOMA.

WE HAVE GROWN FROM SIX POLICY HOLDERS IN 1986 TO APPROXIMATELY 500 IN 1990. SOME GROWTH HAS BEEN FROM COMPULSORY ENROLLMENT, BUT BY AND LARGE, IT HAS BEEN

A MANAGERIAL DECISION ON THE PART OF THE FARMER LISTENING TO ME AS I CITED THE BENEFITS, THE COST, AND THE UMBRELLA PROTECTION OF THE PROGRAM. HIS DECISION BASED ON THOSE FACTS HAVE KEPT MANY INSURED FOR YEARS.

A YEAR AGO, THIS CONGRESS COMMISSIONED 20 RESPONSIBLE PEOPLE TO CANVAS THE COUNTRY AND TALK TO FARMERS, INSURANCE AGENTS, COMMODITY GROUPS, AND OTHER INTERESTED PEOPLE ABOUT CROP INSURANCE, AND HOW TO IMPROVE IT. THAT COMMISSION CAME UP WITH 26 RECOMMENDATIONS TO VASTLY IMPROVE THE PROGRAM AND MAKE IT A VIABLE AND ACCEPTABLE PROGRAM TO THE AGRICULTURAL COMMUNITY. NOW, WITH THEIR RECOMMENDATIONS READY TO BE INCORPORATED, THE ADMINISTRATION IS WANTING TO KILL THE CROP INSURANCE PROGRAM BEFORE THE RECOMMENDATIONS CAN BE IMPLEMENTED. THIS FRUSTRATES AND DISMAYS ME.

WITH THE EVENTS IN EASTERN EUROPE AS THEY ARE, I FORSEE THE POSSIBILITY OF VAST AMOUNTS OF FUNDING GOING TO THOSE COUNTRIES. WE ARE CONCERNED ABOUT BUDGET CUTS AND LIVING WITHIN IT, BUT I'M WARY ABOUT THE FUTURE, ESPECIALLY IN REGARDS TO FUNDING THERE. I FEAR WE WILL INSURE EASTERN EUROPEAN FARMERS IN THE FINAL ANALYSIS BY POURING VAST AMOUNTS OF MONEY INTO THOSE COUNTRIES SO THEY CAN DEVELOP AN AGRICULTURE TO COMPETE WITH MINE. LETS FUND A SOUND, KNOWLEDGEABLE, CROP INSURANCE PROGRAM DELIVERED BY THE PRIVATE SECTOR, INTERESTED IN PROVIDING FOR DISASTERS OF THE FUTURE THROUGH CROP INSURANCE... NOT QUESTIONABLE, HAZY, AND UNPREDICTABLE DISASTER PROGRAMS WHICH MAY OR MAY NOT BE ACTIVATED.

I TRULY THANK YOU FOR YOUR ATTENTION.

Max J. Claybaker

MAX J. CLAYBAKER

Senator PRYOR. Mr. Richard Gibson.

STATEMENT OF RICHARD C. GIBSON, CHAIRMAN, AMERICAN ASSOCIATION OF CROP INSURERS, COUNCIL BLUFFS, IA; ACCOMPANIED BY PAUL FRISKOPP, INSURANCE AGENT, SHELTON, NE, AND RUTH GERDES, INSURANCE AGENT, AUBURN, NE

Mr. GIBSON. Mr. Chairman, I too have a prepared statement, but I think in the interest of time, I would like to place it in the record.

Senator PRYOR. Your full statement will be placed in the record.

INTRODUCTION

Mr. GIBSON. But I would just like to say that I am chairman of the board of the American Association of Crop Insurers and also president of the American Agrisurance in Council Bluffs, Iowa. But probably most important today, with me is Paul Friskopp on my right, who is an agent from Shelton, Nebraska, as well as Ruth Gerdes, on my left, who is an agent in Auburn, Nebraska. Both of these people, who have to deal on the day-to-day basis selling a product, providing risk management to farmers. There is a significant difference in crop insurance that you have to sell where the farmer pays a portion of the premium versus something called disaster where you line up after the fact and only prove your bushels to collect a payment.

YOU CANNOT START AND STOP A CROP INSURANCE PROGRAM

So there is a very significant statement in that you cannot start and stop a crop insurance program. You are going to have to continue to fund this program for 1991. It cannot be dropped, as the administration proposes, and hope you can start it up in 1992 after you come with new legislation. So I urge you as the committee and I also urge the administration to fund crop insurance for 1991 as well as to roll the operating agreements forward with the companies so that we do not have this lag in coverage or a cessation of coverage that may otherwise happen. It is really important that this happen because I think that you will see a significant growth in crop insurance this year, also there are a significant number of lenders who need the collateral of crop insurance to make operating loans.

I certainly disagree with Mr. Kislak and his statement that only 2 percent of the lenders are requiring crop insurance.

SUGGESTIONS

There are four or five suggestions as far as going forward with crop insurance and how to improve it.

First, adequate coverage is needed. We recommend that the ASCS yield should be used as a basic insurance yield with farmers having both the options of the incentive of proving their actual yield, and a pilot program to insure yields at higher than 75 percent of their insurance yield.

Second, a simpler form of crop insurance should be available. As you heard on two or three different occasions this afternoon, a dollar type coverage should be available. An explanation of a dollar coverage proposal is attached to my statement so it can be available to you in your committee and maybe you could make that available to FCIC for us.[10]

Senator PRYOR. And are you also saying that the Federal crop insurance should be available to program and nonprogram crops?

Mr. GIBSON. Yes, very definitely.

Senator PRYOR. Is this the feeling of our group this afternoon?

Mr. GIBSON. Yes.

A third point is the need for an overall restructuring to provide greater flexibility for private insurance companies has to be built in so that additional products can be designed to meet unique needs of farmers in different areas. Mr. Classen indicated companies are willing to take more risk but we cannot be knit picked in the same dogmatic way in which FCIC has done to allegedly enforce the rules in the past.

One of the most essential ingredients in the proposal we have before you is a restructuring of the FCIC; we think that a new agency must be created, one that is independent and will operate the program on a businesslike basis. The bureaucratic problems have been the major obstacles in the past. The new agency has to have a strong administrator. Senator Kerrey, I saw your suggestion for the resolution trust in The World Herald last week, that type of approach with four private members, three government members, and the chairman to be picked from the private sector. I think this has a lot of potential for the Federal Crop Insurance Corporation.

The farmer premium subsidy, must be on a long-term phaseout basis. I do not think that you can immediately fund a self-insurance program without continuing some type of Federal subsidy for the short term.

And finally, the risk-bearing companies, as Mr. Classen indicated, need to take more risk.

I would only like one further comment, and hopefully you will receive some comments from Mrs. Gerdes and Mr. Friskopp, in the February 28 announcement in the Federal Register——

Senator PRYOR. I was going to ask you all about that.

Mr. GIBSON [continuing]. It appears to me that the administration has attempted to protect themselves with the "if funds are available" clause. However, they have warned the farmers that the funds might not be available. However, as a company writing over $80 million worth of MPCI crop insurance, we are left holding the bag. They are asking us to continue to solicit policies, to talk to farmers and tell them that here is a policy that might be available on a "maybe basis" for 1991. We do not know whether there will be funding available for it or not.

In addition, we have expended huge amounts of money to produce those policies, issue those policies, and I think it creates a terribly poor impression to a farmer that you might have coverage, if funding is available.

Senator PRYOR. Were you surprised, by the way, at the language in the Federal Register?

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[10] See pp. 146–147 for MPCI Made Simple—Dollar Coverage Plan.

Mr. Gibson. Frankly, sir, nothing that FCIC does surprises me anymore, however, they should have said that it was the administration and not the Congress who proposed no funding for 1991.

Senator Pryor. This is pretty strongly, it was a rather callous act.

Mr. Gibson. I think it was very callous, sir.

[The prepared statement and attachments of Mr. Gibson follow:]

Testimony of

Richard C. Gibson, Chairman
American Association of Crop Insurers

Before the Senate Subcommittee on
Agricultural Production and Stabilization of Prices

March 6, 1990

Mr. Chairman, members of the Subcommittee, thank you for inviting us to be here today. I am Richard Gibson, Chairman of the American Association of Crop Insurers; and also president of American Agrisurance of Council Bluffs, Iowa. AACI's membership writes about 70 percent of the multiple peril crop insurance and represents both reinsured companies and master marketers.

Throughout rural America, crop insurance is sold and serviced by about 13,000 insurance agents and adjusters; and two of those agents, Paul Friskopp and Ruth Gerdes, affiliate members of AACI, are here with me today.

Mr. Chairman, in 1989, $13 billion of protection was in force on over 800,000 policies, covering over 50 percent of the eligible acres. This was an all time high. Of course, some of this tremendous increase was due to lingering effects of the 1988 drought, the requirement to purchase crop insurance in the disaster act, or a requirement by a lender. But I honestly believe that the vast majority of this new and continued business was a result of the efforts of the private insurance sector.

We're very proud of the fact that we were able to provide this protection and economic security to our rural communities. And, quite frankly, it bothers us when people say crop insurance doesn't work. It has worked in keeping thousands of producers on their farms, with the ability to repay their loans and make purchases from main street merchants.

After the significant progress made during the last two years, it was truly a disappointment to see the Administration's budget and farm bill proposals. We oppose the Administration's effort to eliminate the crop insurance program and replace it with a low level disaster program.

Mr. Chairman, the Administration's proposal has put us back in the position we have so often found ourselves. We make progress, increasing participation, only to be set back by some unnecessary and arbitrary government action. Instead of putting our energies into ways to improve the program and help farmers, FCIC has forced us to reallocate our resources into crisis management -- correcting misunderstandings and dealing with this government-created confusion.

Farmers are unsure whether coverage remains in effect on spring planted crops or whether policies will be cancelled; whether sign up will take place on raisins and citrus; and what will happen for fall seeded crops such as winter wheat if Congress has not completed the farm bill.

It is essential that farmers receive clarification from Washington that the government -- USDA and Congress -- will not abandon the farmer and leave him in some type of "never-never land." Unfortunately, fiscal years, crop seasons, and insurance deadlines do not coincide in the most practical manner. Unless the program and operating agreements are extended or some emergency action is taken immediately and I repeat immediately, for 1991, companies must begin cancelling policies as early as April 30 on a limited number of areas and by June 30 in many winter wheat areas. If this is allowed to happen, agriculture leaders would be unable to provide operating loans to a significant number of farmers.

Because of the critical nature of this problem we would respectfully request that this Committee urge the Appropriations Committee to fully fund the federal crop insurance program for fiscal year 1991. This will allow an orderly transition to any new program created in the 1990 Farm Bill.

As for what should be included in the 1990 Farm Bill, we believe that a restructured crop insurance program is the most equitable and cost effective way to provide disaster protection to farmers. The new restructured crop insurance program should include the following features:

1. Adequate Coverage - During the hearings of the Crop Insurance Commission, the most frequent complaint we heard from farmers was inadequate coverage. A revamped crop insurance program must deal aggressively with this problem. We recommend that ASCS yields should be used as the basic yield, with farmers having both the option and the incentive of proving their yield. In addition, there should be a pilot program to insure yields at higher than the current 75% level.

2. A Simpler Program for Farmers and Insurance People - One of the greatest problems with the current program is its enormous complexity and bureaucratic red tape. We must offer a simpler program under which a farmer can insure his crop for a certain number of dollars per acre, much like he is able to do under the current private hail insurance policies. Farmers will buy a program that is simple to understand and where benefits are known up front. In addition, companies can deliver such a simple program much more effectively than they can the current extremely complex program. A description of a "dollar coverage" program is attached to my statement.

3. Greater Flexibility for Private Insurance Companies -If the farmer is to be best served, the private companies must be given the maximum flexibility to innovate and to compete for farmers' business. Under the current rigid, bureaucratic program, private insurance companies are not allowed to do what they do best -- serve the farmer (customer) in a competitive environment.

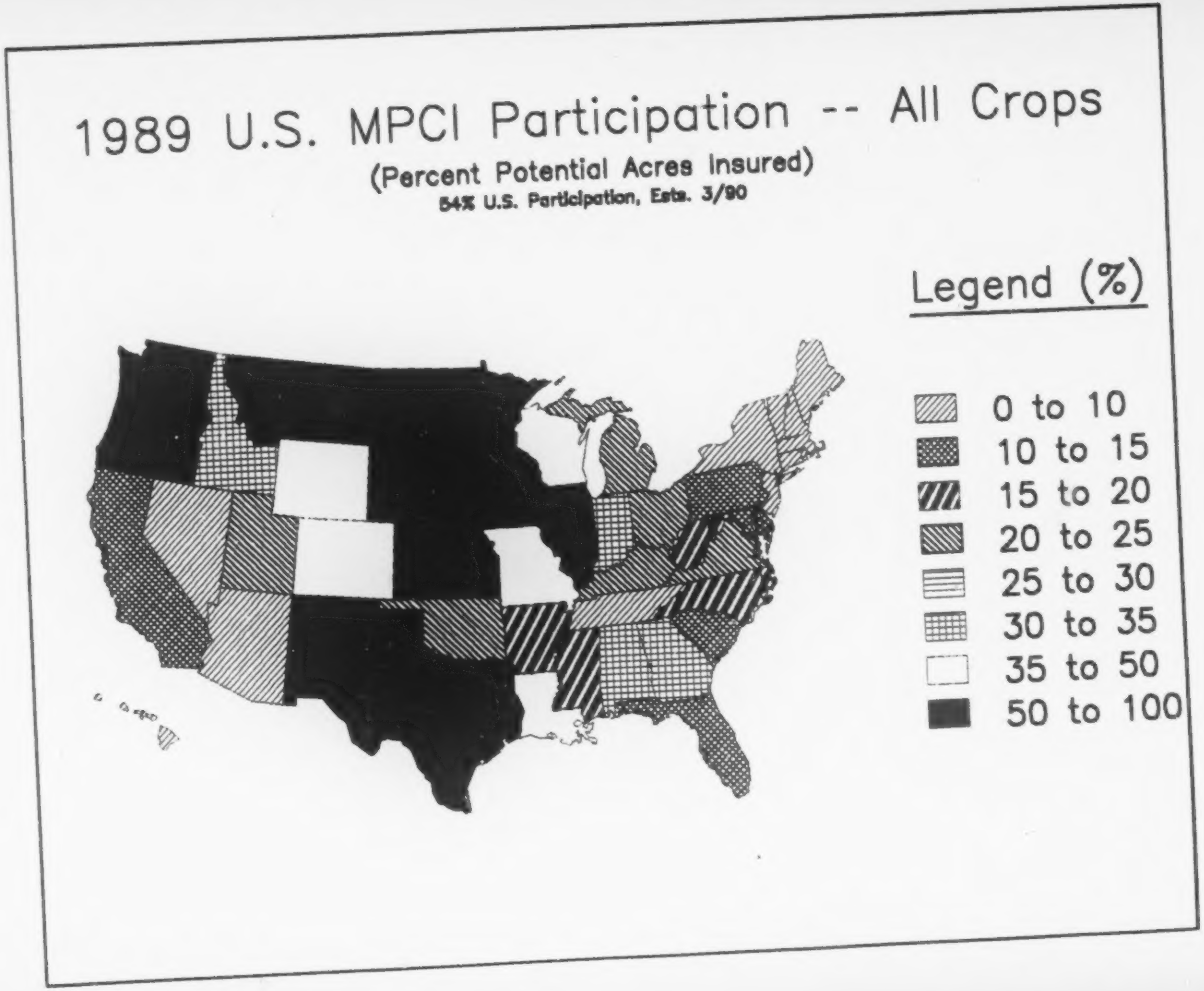
4. A Restructured Federal System - The role of the Federal Crop Insurance Corporation needs to be radically altered and reduced. We are not advocating deregulation, because we know as long as federal dollars are involved, there will need to be federal regulation. However, we feel the role of FCIC should be changed to one of acting as a true regulator, much like state insurance commissions. One of the things that the revamped agency would be charged with is rate approval. Another function would be ensuring that private companies build and maintain adequate reserves.

5. Farmer Premium Subsidy - Obviously, there must in the short run, be federal involvement in subsidizing premiums for crop insurance. However, we feel this could be best achieved by channeling subsidies through ASCS, rather than the FCIC. We feel that it would be better to have ASCS perform the function of issuing vouchers or certificates for the premium subsidies. The most equitable way for this to be done would be for the farmer to receive a voucher to pay for a certain percentage of his premium at whatever level of insurance coverage the farmer chooses to buy.

6. Risk Bearing and Reinsurance - We feel companies can and will take more risk if they are given the proper incentives. Moreover, the companies should take the first dollars of loss, thus insuring integrity in the claims adjustment process. At catastrophic levels, government reinsurance would be necessary. In addition, for certain high risk policies, it will be necessary for the government to provide reinsurance to have an assigned risk program.

Mr. Chairman, we are committed to a sound crop insurance program and offer our assistance in working with the Committee to fashion such a program.

Thank you again for the opportunity to testify and we will be pleased to answer any questions you have.

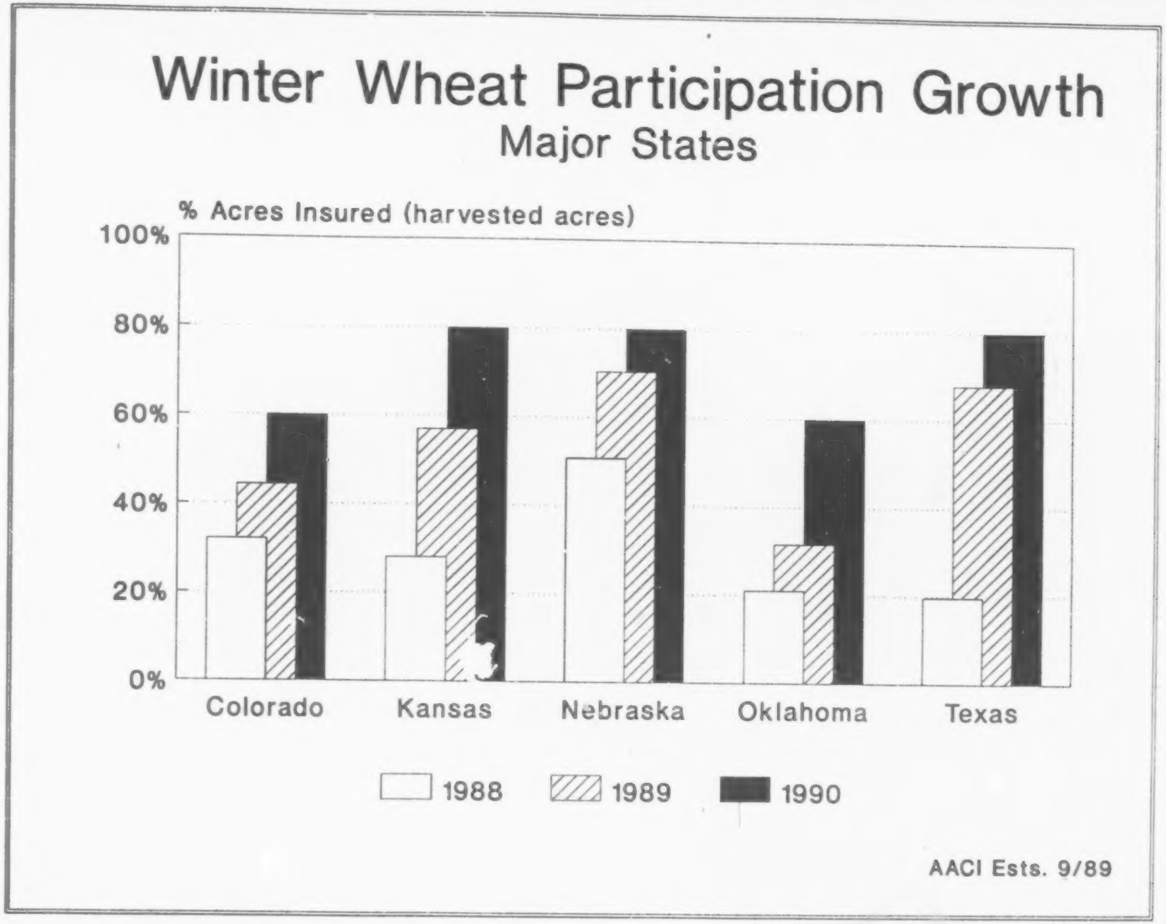


1989 U.S. MPCI Participation -- All Crops

(Percent Potential Acres Insured)

54% U.S. Participation, Ests. 3/90

Legend (%)
▨ 0 to 10
▩ 10 to 15
▨ 15 to 20
▧ 20 to 25
▤ 25 to 30
▦ 30 to 35
□ 35 to 50
■ 50 to 100



Winter Wheat Participation Growth

Major States

AACI Ests. 9/89

MPCI Made Simple - Dollar Coverage Plan

A simple approach to MPCI would be to offer a dollar amount of coverage and pay claims based on the percent of loss (actual yield divided by normal yield).

I. Mechanics

1 **Coverage** is quoted on a dollar basis ($200/A., 250/A., etc.) for a given number of acres (limited to the approximate dollar value of the crop less the deductible). The deductibles for standard plans remain at 25, 35, and 50 percent. The deductibles should disappear when catastrophic losses are experienced. Pilot programs should be initiated at lower deductibles at increased premiums in very stable production areas (i.e. Imperial Valley of CA; Central. IA, etc.).

2 **Premiums** are expressed as a percentage rate.

3 **Premium and administrative subsidy** would be paid by the government to producers. The subsidy could be in the form of a crop insurance certificate given to the grower at ASCS.

4 **Claim is calculated** by multiplying the percentage of insurable loss times the dollar coverage per acre times the lesser of the insured or planted acres.

  a Notice of damage or loss must be filed when loss becomes evident. Visual inspection will be made while production evidence is still available. The producer is advised that production records (including receipts) must be available at the time of final claim that include: date of planting, variety, seeding rates, date kind and amount of fertilizer, date kind and amount of herbicides, elevator settlement sheets, dates of harvesting and by whom, ASCS maps with acreage determinations and etc.

  b The normal yield expectation will be the higher of the APH proven (five most recent years) yield or the ASCS yield for program crops (county average yield for other crops).

  c Percentage of insurable loss is determined by dividing the yield by the normal expected yield, less the deductible times the dollar amount of coverage.

  d Low yield calculation is done by determining the yield for all of the acreage of the crop on the farm. If a grower reported 100 acres but had more acreage, the average yield per acre is determined for whole farm from ASCS maps and sales/storage settlement sheets that the producer has ready for adjuster and certifies to their accuracy and completeness. The producer must understand that the final claim is subject to later audits and penalties for false certification.

II. Example:

Purchased $200/A. coverage with 25% deductible

100 bu./A. normal yield
- 20 bu./A. low yield
80 bu. loss
80% damage
- 25% deductible
55% payable damage
x $200/A. coverage
$110/A.
1.3 accelerated payment factor (100% divided by 75% after deductible)
$143/A. loss payment

III. Other Considerations

1 To strengthen the first line underwriting defense, a portion of the agent's compensation must be based on the insurance experience (loss ratio).

2 Units would be current definition subject to how production records are kept.

3 Yield records would be producer certified auditable production evidence divided by acreage from ASCS maps with crop acreage delineated on them. A hard copy of such records would be attached to the claim form.

Summary

Pros:

1 Simplicity

2 Reduced administrative costs

3 Improved marketability

4 Reduced error rates

5 Improved customer satisfaction

6 Opportunities for flexibility regarding:

  a varying deductibles at different rates

  b speed of payment (increasing payment provisions)

  c pricing based on the reinsurance premium rate (private and/or government)

7 Minimum oversight is required

8 Not much bureaucracy is required to oversee such a program.

9 This would be a significant change from the current MPCI program while maintaining the basic concept.

10 No need for government to establish price elections.

Cons:

1 There would be a program change.

Options:

1 Could use ASCS yield to determine what yield span the grower fits into for rating purposes.

2 This approach to normal yields is approximately 10% higher than current coverage, therefore increased rates would also be necessary.

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3/6/90

Senator **Pryor**. Let us go to our good friend now, Bill Bracey, from Blytheville, Arkansas, and then we will have some questions for this fine panel. By the way, we appreciate you bringing your colleagues here with you here, too, today. May have a question or two. Bill, you sat through this whole hearing.

STATEMENT OF BILL BRACEY, NATIONAL ASSOCIATION OF PROFESSIONAL INSURANCE AGENTS, BRACEY INSURANCE AGENCY, BLYTHEVILLE, AR

COMMENTS ABOUT THE HEARING

Mr. **Bracey**. I am not really short on words, very often, but I feel like I have been to the Super Bowl and sat on the 50 yard line, and all these people have been players and Senator Kerrey and the rest have absolutely said everything I can think of to say. When you get a strong advocate and you see a consensus develop, I have talked myself out of a lot of sales. And by George, I am not going to talk myself out of this. [Laughter.]

The only people that may be players but absolutely quibble with the coach and everybody else is the Department of Agriculture. They would not come to play. They are out on a back fence. But that is the only people that did not seem to be into the spirit of this hearing. Even Senator Bond, at least he has some feelings, you know, about it. We will not get into our problem in the Southeast, but I do want to visit with you about it. I want to acknowledge I am here courtesy of the PIA. I did not pay my own way, but I do pay dues every year. [Laughter.]

I do not, I really do not know how much this ticket has cost me. But I would be pleased to answer any question that I could.

[The prepared statement of Mr. Bracey follows:]

Statement From National Association of Professional Insurance Agents

March 6, 1990

Hearing

Before the Subcommittee on Agricultural Production

and Stabilization Prices

U.S. Senate

Delivered by:
Bill Bracey
Bracey Insurance Agency
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The National Association of Professional Insurance Agents

Who We Are:

PIA National is a nonprofit trade association representing more than 180,000 independent insurance agents and their employees who sell and service all lines of insurance, specializing in coverage for homes, autos and business. PIA is represented throughout the U.S., Puerto Rico and the Caribbean by members affiliated with 42 PIA state and regional associations.

Purpose:

Founded in Washington, D.C., in 193, PIA is one of the oldest and largest insurance associations. Its major goals are to promote the interests and future of its members, and to seek to educate consumers on insurance matters. The association is a leader within the insurance industry in pursuing and advocating consumer-related issues. PIA National's consumer advisor, Esther Peterson, is leading the association's push to help the insurance-buying public.

PIA Concerns:

PIA is firmly committed to the ideal of state regulation of insurance, yet the association recognizes that the federal government plays an increasingly important role in matters affecting agents and insurance consumers. Through its government affairs division, PIA works closely with state and federal lawmakers and regulators to maintain direct input into insurance decisions at all levels of government.

PIA Member Profile:

The typical PIA member is a community-minded business owner with five or six agency employees. This independent agent offers a wide range of insurance products and services, and represents an average of seven insurance companies in order to provide the best insurance protection tailored to the needs of insurance consumers.

PIA members provide more than $3 billion in insurance protection throughout the nation, and average more than $1.4 million in policy premiums written each year.

Independent agents belonging to PIA are often community leaders, active in public service and volunteer organizations. PIA national encourages community involvement by sponsoring public service programs for implementation at the local level. In recent years, PIA and its members have spearheaded campaigns on drunk-driving prevention, the use of child safety seats in cars, arson prevention, installing smoke detectors in the homes of the elderly and handicapped, and Special Olympics.

Typically, PIA members are college-educated and continue their educations to stay abreast of changing market conditions and insurance products. PIA responds to its members' needs with guidance, information and a variety of educational programs to help improve skills for every level of insurance experience--from beginner to seasoned professional.

PIA encourages professionalism and sales excellence through a subgroup, the Society of Certified Professional Insurance Agents (CPIA), which honors the top property/casualty insurance producer in the United States. In 1986, the association sought to further insurance education and research by creating an insurance foundation.

I am Bill Bracey, owner of a small insurance agency in Blytheville, Arkansas. I am an independent insurance agent and have been in the crop insurance business for over 34 years. Ninety-nine percent of my crop insurance business is with reinsured companies and one percent direct Federal paper. I am here representing the National Association of Professional Insurance Agents (PIA National).

PIA National is a nonprofit trade association representing more than 180,000 independent insurance agents and brokers and their employees who sell and service all lines of insurance, specializing in coverage for homes, auto and business. PIA is represented throughout the U.S., Puerto Rico and the Caribbean by members affiliated with 42 PIA state and regional associations. PIA National has members in each state participating in the Federal Crop Insurance Program by selling FCIC-reinsured multiple-peril crop insurance. They also sell hail insurance and can provide farmers and ranchers with a broad range of insurance coverages tailored to meet their clients' needs.

PIA National commends the Chairman for holding this hearing in conjunction with the new farm bill. We welcome this opportunity to present our positions and observations on various aspects of the Federal Crop Insurance Program.

Farming is a risky business and always will be. Crops are subject to many hazards over which farmers have no control. Even in the best producing years, thousands of crop acres are totally or partially destroyed by bad weather, insects and disease.

The farmer faces more inherent risks in his operation than any other businessman and invests more money in a single year than most non-farm families invest in a lifetime. A crop disaster rapidly can become a personal financial disaster putting a farm and farm family permanently out of business.

Ever since the Dust Bowl days of the 1930s, the federal government has played an important and expanding role in helping farmers and ranchers recover from losses suffered as a result of natural disasters. A brief survey of the history of disaster assistance programs for farmers suggests a pattern of generous and pragmatic national responses to specific disaster situations.

Many of the hazards faced by farmers --- floods, droughts and other natural disasters --- not only are largely beyond their control, but most are not subject to coverage by private sector insurance. In the absence of adequate insurance coverage, farmers and ranchers have requested assistance from the federal government with a variety of disaster programs.

In 1978, the Carter Administration asked Congress to broaden the Federal Crop Insurance Program to end disaster payments, arguing that these payments were not equally available to all farmers, were expensive and were encouraging production on marginal land that might better be left uncultivated. Also noted was that almost one third of disaster payments went to farmers who repeatedly planted on land susceptible to natural disasters. So in 1980, Congress decided to scrap direct payments to farmers whose crops were damaged by drought or other disasters in favor of a new subsidized, expanded Federal Crop Insurance Program (Public Law 96-365). PIA was very active in lobbying efforts to develop this program.

The Federal Crop Insurance Act of 1980 provides for the development of all-risk insurance coverage for all major crops that is actuarially sound and based on a unique partnership between the Federal Crop Insurance Corporation (FCIC) and the private insurance industry. The law provides for the use of private insurers to the maximum extent possible to handle the insurance functions supported by FCIC reinsurance. This policy is designed to prevent an ever-expanding FCIC bureaucracy and encourage utmost efficiency by utilizing the wealth of technical and marketing expertise by both insurance companies and insurance agents.

The provisions of the new program of most interest to independent insurance agents and brokers were those that directed the FCIC to market and service federal all-risk insurance through agent associations, private insurance companies and licensed agents and brokers, and to pay them administrative expenses, including commissions and any legal costs incurred should they be held liable for FCIC errors (hold-harmless agreement). The Act's entire thrust is keyed to the maximum utilization of the private insurance sector and PIA whole-heartedly supports and will diligently work to help achieve the success of this effort.

Mr. Chairman, PIA is deeply concerned about the Administration's proposal to eliminate the Federal Crop Insurance Program and to replace it with disaster assistance program. We recognize the concerns about the program's low participation and its cost to the taxpayers. However, federal crop insurance can provide assistance more equitably and efficiently than the emergency loan and direct payment programs.

Federal crop insurance gives farmers control over the extent of their protection: the benefits are known before damage or loss occurs; the federal government spends less money on crop insurance over time than it does on other disaster aid programs; and the net result is a savings to taxpayers. The General

Accounting Office (GAO) confirmed this in their September 1989 report to Congress. The GAO report said that compared to the three forms of disaster assistance currently provided --- direct cash payments, loans and insurance --- the crop insurance program can provide assistance more equitably and efficiently. GAO also found that despite the intentions of the 1980 Act to alleviate the need for ad-hoc disaster assistance programs, crop insurance has been competing throughout the 1980s with direct assistance and loan programs that have received larger amounts of federal funds and have had more attractive terms for farmers. GAO recommended that a restructuring of the agriculture disaster assistance programs that removes these disadvantages could help determine the effectiveness of the crop insurance system.

PIA National believes Congress needs to address the balance between farm disaster loans and its Federal Crop Insurance Program. In order for both to work, there has to be a requirement that farmers be aware of the program. Congress needs to tell farmers that this is available and if they don't avail themselves of this protection, there are going to be consequences that they have to face affecting them individually or may apply to them collectively in the form of a disaster in a farm community.

In this regard, PIA is more than willing to work with the FCIC and other groups that goes out to farmers to teach and inform them of how they can better manage their exposures. We will participate at the local level, county level, state level, regional level and national level. We'll work with you in designing programs. PIA has a membership base that touches all of these farmers.

Do our people have something at stake? Yes. Our people sell the product. Yes, we make a commission, but more importantly, our people sell a whole bunch of products. They are the insurance agents of these farmers for their other coverages.

The fact that you paid out all those billion dollars in federal disaster payments is not a failure of the Federal Crop Insurance Program. Did the Federal Crop Insurance Program over the last ten years have a real fair shot at getting established? The answer is No. You had a program that was constantly changing. It was being introduced to farmers at the beginning of its life cycle with predominantly the "old school" farmers who were tough sell on any insurance. The farming community in the 1980's was going through problems with over extension of credit and going out of business and couldn't afford enough money, but, nonetheless, the federal crop insurance program took off.

Buying into the Federal Crop Insurance Program is a business decision. With adequate coverage and acceptable pricing, you're going to be able to sell the program because today's farmers recognize more than ever that they put more risk in one year than farmers ever had in the past so there is less ability for the farmers to say we'll wait until next year. Farmers have to make every year count. Unless you provide federal crop insurance, you're not going to allow every farmer to gain that protection.

Farmers, above all else, are people who wish to say that they are self-sufficient. The Federal Crop Insurance Program gives them an additional tool to continue that self-sufficiency to protect their interest to the extent that they believe they economically must be protected. Additionally, farmers are small business people, very similar to independent insurance agents. They are becoming more astute business people; are understanding better the financial management and the element of risk not just as an agricultural or meteorological happening, but as definite effect on their economic viability and survivability.

Farmers are also tough clients to sell - whether you're selling them a Commercial General Liability policy, or federal crop insurance. It's a little harder to sell them crop insurance because they are confident that in the event of a disaster, the federal government would provide relief regardless of whether a farmer had insurance or not. The 1988 drought was a perfect illustration. With only 13 percent of the nation's estimated 3.3 million farmers relying on government-subsidized insurance, they collected $3.9 billion in direct aid and an additional $1.1 billion in crop insurance.

In conclusion, PIA National:

- Believes that the Federal Crop Insurance Program is a program designed first and foremost to protect the American farmer. Farmers participating in the program enhance the stability of the local economy in a given agricultural area.

- Recognizes that the crop insurance program is not now, nor was it ever designed to be a cure-all for the broad range of economic problems that on occasion adversely impact agriculture.

- Agrees that a crop insurance program cannot be effective as long as there is the potential for large disaster payments, and that any reforms must stem the political pressure for ad hoc disaster legislation. Current program losses are expected to remain high until lower risk producers are attracted to the program.

- * Believes that the program is still evolving. If the program is to meet producers' needs, those engaged in its operation must be constantly alert to many factors. Not only changes in the weather, but changes in the political climate affect the program.

- * Major improvements to this federal insurance program have been possible because of the government-private industry partnership. It is PIA National's opinion that a key to success of the Federal Crop Insurance Program is the maximum possible use by the FCIC of the private insurance sector.

- * Continues to stand ready to work with Congress, the U.S. Department of Agriculture and other agencies to protect the American farmer by providing the necessary insurance coverage to protect the stability of our local and national economy.

Mr. Chairman, we need your help and support of the Federal Crop Insurance Program. While not perfect, crop insurance works.

LMA:2/23/90:lma072

Senator PRYOR. Bill, by the way, have you seen, since the Federal Register came out last Wednesday, have you seen, or has it had time to sort of filter out? Have you seen any sort of a change since the Register has come out or has it had time to take effect?

Mr. BRACEY. This whole thing—you know I have been in sales for 34 years. I have never lived on anything but a commission except when I was invited into the Korean war. This program has been a challenge because it is so well conceived and had good intent. It was clear the intent of the Congress, but it has been the biggest mess to get on the road that I have ever seen. You sell somebody something and they change the program after you sold it. You know how this then would come out—if our companies—and I represent a lot of big insurance companies—if they sent out a notice to all my policyholders saying we may not have any money, why, hell, they would be cut and run. They would be gone.

Fortunately, they do not take these people's word because they have cried wolf too many times. And so they just think that is part of the game. But, no, it is not going to hurt so much because our participation is so low in Arkansas and Mississippi.

Senator PRYOR. What about the credit aspect of Federal crop insurance when you borrow money, a farmer?

Mr. BRACEY. Your friend, "Bo" Huffman, reluctantly, you know, he did not think much use of the program until it was explained to him by the fellow that owns these banks. It changes the very nature of collateral. You go in to make a loan at a bank and they look you straight in the eye and say we do not make crop loans. They tell you that, but they do not release the crop. When you insure that crop, you change the nature of that asset to cash money, either production or the Government pays it. It took a long time for the bankers to look into the program and what it could do. John Minor told me he sent you a lot of data. John works, and he has had a crusade of explaining to the bankers that crop insurance is a good tool for the bank.

Now there is not enough protection there to really help the farmer, but it helps the farmer if he is able to get financed again next year, and he would not be able to get there without it. Now if he draws on crop insurance two or three times in a row, he is going to be broke anyway. Because the price of the commodities, if you make an average crop on soybeans, you may not come out in the black anyway. You must lose 25 percent of your crop before you can benefit from the program. They talk about participation is the key to insurance. I would be for more subsidy in the program if it would sell more insurance. I think talking about getting rid of subsidies is self-defeating.

Senator PRYOR. Senator Kerrey, we have a panel of people here who are on the front line every day in this war, in this battle. Please feel free to ask any questions at this time of the panel.

Senator KERREY. Well, the question I would ask all of you is whether you think it is possible at some point, if we implement the recommendations that have been made, and in particular, if we devise some restructuring strategy that permits the program to be operated well, is it possible for this program to become self-sufficient, self-sustaining? We know it is desirable, but is it possible for it to become self-sustaining?

Mr. **GIBSON**. Yes, Senator, I think it is, but it is not going to be immediate. I think you are going to have allow a transition from the current to the new program and it may take 3 to 5 years down the road to see significant results. You can increase the premium to the farmer dramatically, say from $3 to $9 per acre, and expect them to buy it immediately. The Crop Insurance Commission and many farmers say they are willing to spend more of their dollars to buy the meaningful protection.

Senator **PRYOR**. Is there a mentality out there among farmers when they are trying to, let us say, choose between Federal crop and nothing? Do they sort of assume that the Federal Government, if there is a disaster, is going to come in there and at least make them whole to some extent?

Mr. **BRACEY**. If they could hear what went on here today about this zero budget business, they would not sleep tonight, but they do not pay any attention to it. They do not believe it will happen. It has already happened. I mean we have made exceptions maybe, but it seems to me the intent is clear that we are going to be out of the disaster payment business. It is just a matter of when because of this nine to one urban majority in Congress.

Senator **PRYOR**. There has been some recent polling data, especially since Senator Moynihan has introduced his bomb shell, as we say. He has thrown the handgrenade into the foxhole on Social Security Trust Fund usage for operation of the Federal general governmental functions. Since that time there has been extensive polling data in those age categories between like 26 to 45. A lot of that age category, they say, does not believe there is going to be any social security money for them when they get to be 45. And then they say, well, are you worried about it? And they said, well, not too much, because I think the Government is going to take care of me. Now is this same sort of mentality out there in the agriculture sector?

Mr. **CLAYBAKER**. Senators, I think I might speak to that.

Senator **PRYOR**. Go right ahead.

Mr. **CLAYBAKER**. I am a farmer and talk to other farmers everyday. I started in this crop insurance business in 1986. I started with six policies. I now have over 500 policies and it has not been due to compulsory crop insurance. In Kay County where I live in Oklahoma, we now have 62 to 69 percent participation, and it has been due to managerial decisions. Now, Senator Kerrey, you mentioned awhile ago these recommendations again. Glenn English is from my home State, not my district, but my home State. And I have some people insured in his area, and one of these recommendations addresses his basic problem. I have a man out there insured for 9 bushels of wheat per acre. It costs him $7 an acre. My neighbor has 24½ bushels per acre guaranteed at $2.65 per acre cost, and that is an actuarial problem. We cannot get away from because of the FCIC rates and rules that we have to live with.

Those things have to be corrected. One of the Crop Insurance Commission recommendations was to establish a separate ASCS yield, program yield for crop insurance purposes only. The one he has presently for generic payments and deficiency payments, that stays. But we do need to address those problems. I am just amazed that Congressman Glenn English is really working so hard to give us a very fine crop insurance program when his constituents are getting less in Oklahoma than mine are.

Senator **Kerrey**. Well, the question really gets to the short term problem, it seems to me, that we are facing, and that is whether or not to go with crop insurance. I think that crop insurance is vastly preferable and I am prepared to make that selection as opposed to annual disaster payments notwithstanding the risk that Senator Bond mentioned earlier. I think that is a significant risk that is always going to be there. But until somebody suggests how to correct the defects in representative democracy, we are going to have to live with that.

Is it going to be necessary and desirable, do you think, in the short-term given what we heard so far here this afternoon for us to make some sort of effort, coming from the Congress, to indicate that we prefer crop insurance as opposed to the disaster program being recommended by the administration?

Ms. **Gerdes**. I would like to address that as a farmer and an insurance agent. And I got into being an insurance agent because it was either my husband and I pack up and go to the city and work, or have some outside income. Right now we have an urgent need for you to pass a resolution that funds and extends crop insurance through 1991. If we do not have that resolution, the decision will have been made for us (there will likely be a lapse in coverage for some 1991 crops). And I do not think that is what anybody here wants. I know that is not what my farmers want. And I work in four States with 800 farmers. Not one policyholder last year received more from disaster than they did from crop insurance. In fact, in 1989, 73 percent of my clients' income came from crop insurance; 27 percent came from disaster.

We paid out $3.1 million. Now that is $3.1 million we paid out. We also collected $850,000 in premiums. So there is some discrepancy and some thoughts there that you are just giving away $3.1 million. That does not happen. In 1989 on crop insurance, one of my farmers received $79,543. Under the proposed legislation that Secretary Yeutter came out with, this same farmer would have gotten $5,903. He would have been out of business. Mr. Kislak and I must talk to different farmers and different bankers. I would like to have on the record that I brought many letters from both lenders and farmers. The lenders that I deal with which are five banks in southeastern Nebraska tell me 175 farmers in Nemaha County would be out of business without crop insurance.

The only way we can stop that in the short-term is a resolution to extend funding for crop insurance into 1991 and fix the problems in the 1990 farm bill.

Senator **Pryor**. Very fine statement. Yes, sir.

Mr. **Friskopp**. My name is Paul Friskopp. I am an agent from Shelton, Nebraska. I would also like to——

Senator **Pryor**. I think by the way that probably is our vote, but we will have to leave in a moment.

Mr. **Friskopp**. I just wanted to add that we have to address some serious problems with the program itself, and I think we can look at the track record since the private industry's involvement in this program since 1980—or I started in 1981, and that is that we were given a program that had been in existence for 50-some years and had participation of barely 10 percent. We have brought that figure up to about 50 percent participation at this point in time with basically two improvements, the separate farm insurance units and the APH program. And I think that if the recommendations of the Crop Insurance Commission are followed, I think we can achieve the participation goals that you are looking for.

And I welcome that challenge. I have worked with producers in the middle part of Nebraska where it is irrigated. There is not a risk of drought, and yet they buy multiperil crop insurance because it is a risk management tool that works. And if we put some kind of a floor into this program so that the ASCS yields would be the bottom limit at which the yields could go down to, I think you have taken a big step in solving the participation problem.

Senator **Pryor**. For me this has been an extremely educational afternoon. This has taken a little over 3 hours, and I have a sense, I tell my colleague Senator Kerrey, the former Governor of Nebraska, that I have a sense that we could get the group who has come here this afternoon to make these statements throughout the afternoon, I think on some Friday afternoon if we all left town together on a bus and met over a weekend somewhere, Sunday afternoon we could come back to Washington and have a fairly good program in mind.

I have a sense there is a sort of a meeting of the minds here with a lot of people. And who knows, maybe we will try something like that. I think there have been some very positive contributions this afternoon. I will be honest with you. When I came to this hearing, I did not think there was a way to—I did not see a way to try to solve this. But I think there is a lot of will out there, and I know that Senator Kerrey has expressed eloquently his will to be a part of this, and we are just so appreciative of all of you coming. I will just finally say that one, and I am fascinated, by the way, with the proposal for a resolution. That is a fascinating development here.

Ms. **Gerdes**. I would like to say on the resolution, that goes back directly to the farmers. My farmers are scared to death.

Senator **Pryor**. Right. And this Federal Register notice doubled scared them.

Ms. **Gerdes**. And that is why that resolution came. That is right.

Senator **Pryor**. And let me also say that one reason, Bob, that I had my good friend Bill Bracey from Blytheville, Arkansas, and one reason I put him last, I wanted him last on the list, and he was last on the list. I wanted Bill Bracey to know that I am up here earning my salary. [Laughter.]

And I want Bill to go back home around Blytheville and tell everyone that old David Pryor is up here, and I finally see what he does with all his time. So this has been a very, very constructive hearing. Senator Kerrey, did you have a final comment?

Senator **Kerrey**. My final comment, Mr. Chairman, is to echo your statement. I have learned a great deal from the witnesses and what has been presented. I see the task as being threefold:

First, is to have the Congress make some sort of a statement, perhaps through the suggested resolution, so that we can, over the next several months, give crop insurance under its current structure a fair chance.

Second, my hope is that we are able to put together this year legislation that will not bust the budget, and that has as its object the implementation of some reforms to crop insurance that will make it work.

Third, the structure that we put together must permit us to do what I think is extremely important and that is work toward gaining not just the trust of the producers that have purchased the insurance but the taxpayers who give us permission to put the program together. That has been extremely difficult for us to do. It has been very frustrating for me just in the short time that I have had the pleasure of serving in the Senate to get the kind of accountability that I think both the taxpayers and the purchasers of this product need.

So I hope we are able in three rather simple steps, without the need to reinvent the wheel, to improve the program. We have good recommendations in place. It seems to me we can make this an awful lot simpler than what might appear on the surface, and I hope, Mr. Chairman, that this hearing provides a basis for doing that.

Senator PRYOR. I think it will.

Also we have a statement from Ralph D. Beal, president of Master Marketers' Association of America, and a statement from George F. Vohs, president of LongView Insurance Companies. These will be placed in the record as well.

[The prepared statements of Mr. Beal and Mr. Vohs and the Federal Register interim rule follow:]

A PLAN FOR THE IMPROVEMENT OF THE FEDERAL CROP INSURANCE PROGRAM.

MASTER MARKETERS' ASSOCIATION OF AMERICA
HONEY GROVE, TEXAS 75446

FOR RELEASE ON DELIVERY
OF TESTIMONY
EXPECTED AT 2:00 P.M.
MARCH 6, 1990

STATEMENT OF

RALPH D. BEAL, PRESIDENT OF MASTER MARKETERS' ASSOCIATION OF AMERICA, CROP INSURANCE PROFESSIONALS OF AMERICA, AND SOUTHWEST CROP INSURANCE AGENCY, INC.

BEFORE THE

SENATE SUB-COMMITTEE ON AGRICULTURE, NUTRITION AND FORESTRY FOR AGRICULTURAL PRODUCTION AND STABILIZATION OF PRICES

ON

THE FEDERAL CROP INSURANCE PROGRAM

MR. CHAIRMAN AND MEMBERS OF THE SUBCOMMITTEE:

The Master Marketers' Association of America is a not for profit association of twelve (12) Agency Sales and Service Contractors who sell and service Federal Crop Insurance paper. The Association promotes the preservation and expansion of the crop insurance program through public information and educational activities and by providing technical assistance and information to the appropriate governmental bodies. In 1989, agents represented by these contractors serviced 99,913 policies covering 204,000 insured farm units across the United States. Insured acreage on these farms exceeded 15 million and the collateral value of these policies exceeded 1.3 billion dollars. My testimony today not only reflects the views of our Association, but also the needs and concerns of the 100,000 active and insured farm operators we service.

The Federal Crop Insurance Program does not need a major overhaul! However, it does need fine tuning and some common sense applied to create a dynamic and farreaching crop disaster protection program.

The Federal Crop Insurance Act of 1980 was passed establishing a comprehensive crop insurance program in all counties. It was the intent of Congress to replace ad hoc disaster assistance programs with an expanded crop insurance program which included more crops and a larger part of the country. Since 1980, crop insurance participation has continued to increase despite the continual implementation of the ad hoc disaster programs by Congress.

Also since 1980, a number of mistakes have been made by the management of the Federal Crop Insurance Corporation, but this can be corrected with positive legislative direction requiring the management of FCIC to implement a viable and positive crop insurance program.
ernmental bodies.

The present debate of crop insurance vs. ad hoc disaster makes little sense. The ad hoc disaster program will not provide production guarantees, it will not protect the farmers in isolated disaster areas, it will not provide loan guarantees and a disaster program will not be as cost efficient as an improved crop insurance program. A farmer should be given the opportunity to buy protection to coincide with his farm operation on a business like basis and not turn to Congress each time a major disaster occurs. The establishment of an improved crop insurance program will eliminate the need for this emergency legislation.

A viable marketing system is required if a program of crop insurance is to achieve participation levels that are high enough to curtail future emergency legislation. Presently over 50% of the acres farmed are insured by multi-peril crop insurance. Prior to 1980, sales were made by salaried FCIC personnel and at one point salaried ASCS personnel represented crop insurance, but neither were successful nor would they be successful in the future. The desire to succeed of personnel willing to work on a commission is the main difference in marketing results.

The crop insurance program should be restricted to a level of government assistance so as to retain and not eliminate the insurance programs now available by private hail insurance. Farmers have been using a combination of crop insurance and private hail insurance for many years, and we would be very concerned if either one were not available.

The stability of the U.S. economy is directly affected by the strength of the farm economy; therefore, a government supported crop insurance program is of vital importance to the farmer. Administration of this program can be managed by the private sector but safeguards must be provided to assure that both the taxpayer and the farmer are protected.

A primary concern of the insured farmer is his premium dollar and the present bail out of Savings and Loans is a grim reminder of the lack of regulation oversight. FCIC should not be allowed to fall into this dilemma. However, a number of GAO reports has brought attention to the lack of fiscal oversight by FCIC.

With the concerns mentioned above, following is a plan for the improvement of the Federal Crop Insurance Program. With this plan farmer participation will increase, their benefits will improve, premium cost will be lowered and the administrative costs to taxpayers will be greatly reduced.

I. **Improve the delivery system by adopting one basic sales and service agreement for all entities who are involved in the delivery of Multi-Peril Crop Insurance to farmers.** (Exhibit A)

The present dual - delivery system of Sales and Service Contractors and Reinsured Companies should be replaced by one private industry delivery system. An applicable name would be "General Agent Sales and Service Contractors" and should consist of the following terms and conditions.

The "General Agent Sales and Service Contract" would specify the qualifications for sales and service of Multi-Peril Crop Insurance. These qualifications should be similar to the Agency Sales and Service Agreement presently being offered by the FCIC.

Additional services would be offered by an addendum to the basic "General Agent Sales and Service Contract". Such additional services, as approved by the FCIC Board of Directors, and implemented by the FCIC Manager would be offered to all contractors who would comply with the established qualification requirements for the additional service.

This single - delivery system of sales and service by the private insurance industry would treat all contractors equally and would compensate all contractors the same for services rendered. This would eliminate the present struggle between the two delivery systems that has truly retarded farmer participation.

Currently, there is an excellent network of independent private insurance agents selling and servicing crop insurance. As independent agents they can represent any entity that has a contract with the FCIC. Presently, Agency Sales and Service Contractors and Reinsurance Companies compete for these agents and the proposed single delivery system of "General Agent Sales and Service Contractors" will continue this competition but on a level playing field with respect to commission and services performed.

The present FCIC Reinsurance Contract requires that the contracting company comply with insurance laws and regulations in each individual state in which the company represents the Multi-Peril Crop Insurance Program. These rules, regulations and financial qualifications are very restrictive, and limit the number of companies that can or will qualify for the contract. This is evidenced by the fact that, the number of participating reinsured companies has reduced from forty-seven (47) in 1984 to twenty-eight (28) in 1989. The proposed "General Agent Sales and Service Contract" would be regulated by the FCIC and not the individual states. This would provide the opportunity for an increased number of "General Agent Sales and Service Contractors" to properly train agents and supervise sales and service which will generate increased farmer participation. Furthermore, the implementation of the single - delivery system will simplify the complex dual delivery system presently offered by FCIC, and would substantially reduce the delivery costs for Multi-Peril Crop Insurance.

II. **Appoint an FCIC Board of Directors who are capable and dedicated to the improvement of the Multi-Peril Crop Insurance Program, and who do not have the goal of promoting special interests.**

Since 1980 Farmers have had very little representation on the FCIC Board of Directors. The directors have predominately been individuals oriented to consider the interest of the private reinsurance companies without regard to the effect their decisions have had on farmer benefits and costs, the marketing of crop insurance, the tremendous increase in administrative costs since 1981, and the damage to the structure and operation of the Federal Crop Insurance Corporation.

The present situation dictates that the FCIC Board of Directors be capable, knowledgeable and fair minded. Potential board members should be carefully screened to make certain that if appointed their decisions would be honest and impartial. The interests of the farmer, the Federal Crop Insurance Corporation, the private insurance delivery system, and the costs to the taxpayer would be properly considered.

III. **Direct FCIC to appoint an Advisory Committee to implement recommendations for the Improvement of the Federal Crop Insurance Program.** (Exhibit B)

An Advisory Committee is in the process of being organized and appointed to advise the Congress, Secretary of Agriculture and the FCIC Manager and Board of Directors on matters related to crop insurance. This committee will be an invaluable asset as a stabilizing factor as the FCIC responds to the needs of farmers and policyholders.

IV. **Mandate that FCIC retain oversight on all entities delivering Multi-Peril Crop Insurance with the capability and authority to perform adequate reviews. Thereby assuring proper compliance with rules and regulations.**

FCIC should establish greater oversight on all contractors selling and servicing Multi-Peril Crop Insurance. Presently, FCIC administers a system of compliance review; however, the utilization of this system has been limited. To assure proper compliance with rules and regulations all sales and service entities and loss adjustment procedures should be reviewed regularly. The General Accounting Office (GAO) has reported many past rules violations which have been extremely costly to the taxpayer. Proper adherence to a strict compliance program will reduce costs significantly.

V. **Eliminate the risk-sharing provisions that now exists for Reinsurance Companies which allows for profits at the expense of insured farmers with excessive costs to FCIC.** (Exhibit C)

The Federal Crop Insurance Act of 1938 provides for private insurance companies to enter into a Reinsured Agreement with the Federal Crop Insurance Corporation on an experimental basis. If there is to be risk bearing it should be under that provision, and should be with conditions fair to the private company and the FCIC. The FCIC was structured to bear the risk in the 1938 FCIC Act and did so in a very satisfactory manner

through 1980. During that 41 years of experience the FCIC carried all the risk; nevertheless, a reserve of $60,000,000 was achieved.

The present risk sharing provision now being offered by the FCIC as a part of the Standard Reinsurance Contract should not be included in the single - delivery "General Agent Sales and Service Contract".

VI. **Establish and maintain a central data base administered by FCIC accounting for the complete loss history and identification of all policyholders.**

FCIC should establish and maintain a central data base accounting system for crop insurance experience and identification of the individual policyholders to include all contractors. Since, no such system exists insureds and contractors have abused the crop insurance program resulting in excessive cost to the taxpayer.

VII. **Assign all actuarial and underwriting responsibili-**

ties to FCIC and disallow all interventions by private Reinsurance Companies.

FCIC should continue to be responsible for all actuarial and underwriting activities. This responsibility should not be placed in the hands of any entity that sells and services crop insurance unless that entity is assuming 100% of the risk involved.

VIII. Require that all sales and service agents and loss adjusters be trained, tested and certified by FCIC.

To restore stability and integrity, the FCIC should require that all sales and service agents be properly trained, tested and certified by FCIC. This would be accomplished before the respective agent could represent the Multi-Peril Crop Insurance Program. Presently, agents for Reinsurance Companies are not required to pass an exam evaluating their knowledge of crop insurance. The same can be said for loss adjustment training, the loss adjusters for Reinsurance Companies are not tested for knowledge and no formal training program for certification exists.

FCIC maintains an excellent training, testing and certification program for both agents and loss adjusters. This procedure should be mandatory for all contracting entities.

IX. Mandate that all loss adjustment be performed by FCIC or by trained and certified loss adjusters.

Crop loss adjustments are performed by the FCIC and Reinsurance Companies. FCIC performs this function only on federal policies using contract loss adjusters who have been trained and certified according to FCIC procedure. These loss adjusters are carefully supervised by FCIC personnel. During the 1989 crop year the FCIC system of loss adjustment operated at near perfection. Loss adjustments were accomplished within seven days after notification of loss and the vast majority of the farmers had indemnity checks within thirty days of the notice of loss.

Reinsurance Companies are responsible for conducting loss adjustment for these particular companies; however, there is no formal or coordinated effort by the FCIC to train or supervise these adjusters. This results in considerable latitude in their loss adjustment system and creates inconsistencies between companies as well as individual farmer losses.

The GAO report dated November 20, 1987 indicates that Reinsurance Companies (1) did not adjust 95 percent of 134 sampled claims in accordance with FCIC policies and procedures; (2) should not have paid about 31 percent of the $9.4 million in claims (3) may have intentionally overpaid claimants and (4) made incorrect determinations of production guarantees, actual production, payment amounts and program eligibility.

A consistent and systematic loss adjustment system is essential. The most prudent way to achieve such a system is to require that all loss adjustment be performed by FCIC. An alternative to this position would be to allow the "General Agent Sales and Service Contractor" to perform loss adjustment procedures as an additional service subject to approval by the FCIC Board of Directors and FCIC Management. Contractors approved for the additional services option would be required to use loss adjusters trained and certified according to FCIC procedure. This pragmatic approach to loss adjustment will provide stability and credibility. Therefore, significantly reducing the possibility of indemnity over and under payments.

X. **Utilize establish yields as determined by the Agricultural Stabilization and Conservation Service (ASCS) to determine insurance protection and premium cost for each crop. Implement an optional Actual Production History Program (APH) for those farmers who choose to maintain actual records of production.**

ASCS established yields would be used to determine a farmers insurance protection and premium cost after the ASCS yield has been factored to achieve actuarial soundness.

A simplified optional APH plan should be implemented for those farmers who wish to maintain actual records of production. The present mandatory APH program is an administrative nightmare for insureds, agents and contractors and has limited farmer participation.

XI. **The thirty percent (30%) subsidy should be applied to the seventy-five percent (75%) level of coverage (legislation required).**

The increased subsidy participation will encourage farmers to select a coverge level that will recover their crop expenses. Currently, only the 50% and 65% levels are subsidized by 30%. This has encourage participating farmers to purchase crop insurance protection at lower levels of coverage to obtain the maximum subsidized preium.

This situation has sent the wrong message to the farmer, as most farmers complain that the coverage provided by the 65% level does not cover expenses. Offering the 30% subsidy on the 75% level will encourage farmers to select the proper level that will realistically idemnify their expenses.

XII. **The FCIC should adopt a standard insurance policy for all insureds.**

A standard FCIC insurance policy should be adopted and all "General Agent Sales and Service Contractors" selling and servicing Multi-Peril Crop Insurance would offer this policy. The FCIC should also be responsive to farmer needs and requests as policies are developed. In many instances FCIC and the Board of Directors have dictated to farmers their specific needs without consulting individual farmers and commodity organizations.

XIII. **FCIC should implement an optional dollar protection program designed to cover cost of production.** (Exhibit D)

A cost of production option can be offered on a specific dollar basis not to exceed the target price on program crops or similarly established prices on other crops times a specific guarantee of production. The guarantee of production would be the APH yield or the ASCS established yield factored to achieve actuarial soundness.

XIV. Establish an equitable crop insurance program for fruits, nuts, vegetables, melons and other perishable and or fresh market crops.

Attempting to insure crops such as fruits, vegetables, nuts, melons and others perishable and/or fresh marketed crops under the guaranteed production concept invites serious problems. Early attempts to insure such crops under the "guaranteed success" or APH concept against multiple perils have been criticized for a variety of legitimate reasons. Among them are:

1. No adequate source of past records of yield.
   a. Many are marketed direct.
   b. Many are quite volatile in fruiting characteristics.
2. Often Multi-Peril Insurance (guaranteed success) has caused an excessive increase in new growers which often disrupts the sensitive supply-demand equilibrium within local markets.
3. Resulting price volatility often disrupts harvesting/marketing plans (without regard to any adverse effects on the crop caused by nature).
4. Catastrophic events such as hard freeze or hurricane totally distort the yield history base thereby rendering insurance offers in subsequent years virtually worthless in terms of security to the producers.
5. Actual money lost by damage to such crops is directly related to the stage in crop production at which that damage occurs, and bears little or no relationship to the historical yield potential or the unit price to be received in the market place for that crop that year.

Based upon these and, no doubt, other factors peculiar to this category of crops, another plan of insurance should be allowed by legislation. It would seem that a scheme based on insuring a specific amount of production cost, relative to the specific crop in that area, against loss of actual investment from a few, purely catastrophic named perils would better meet the need. Those covered perils should be limited to freeze, wind, excessive moisture (rainfall or flood), drought (for non-irrigated) and unprecedented/uncontrollable disease or insect destruction. In the event the insured commodity is lost to one or more of these perils, the percent of damage/loss would be established and the indemnity based on application of the percent of loss to the maximum insured liability for the acreage, but not exceeding the actual, documented investment in the crop at the time of the loss. Salvage would remain with the insured.

XV. **The premium discount for good experience should be reinstated as an incentive for the insured and continue his crop insurance protection.**

The discount for good experience will encourage continued participation of insured farmers, and also promote crop production rather than crop losses.

XVI. **Maintain present FCIC personnel levels but reorganize the corporate structure to accommodate increased oversight and quality control responsibilities.** (Exhibit E)

FCIC's current resources, both personnel and financial, could be refocused to provide greater support for a single - delivery system with greater oversight and control of program administration. The present dual - delivery system, the independant adjustment of crop losses by Reinsured Companies, the dependence on a complicated Actual Production History Program and other such unmanageable aspects of recent FCIC operational policy has greatly diminished the corporation's capacity to control. With modification of each operational area, as has already been suggested in this plan of improvement, FCIC could redirect its resources to better assure;

1. more consistent representation of the product,
2. better training for agents and adjusters,
3. a more objective and less complex system of farm yield determination,

4. a more established and constructive oversight and compliance function, and,

5. reduced dissatisfaction most often related to differing offers and benefits perceived to be available through different delivery points.

XVII. Eliminate ASCS ad hoc disaster programs.

> Most farmers would purchase Multi-Peril Crop Insurance if Congress would refrain from passing ad hoc disaster programs.

The Federal Crop Insurance Act of 1980 was enacted to provide a comprehensive crop insurance program. The intent of the Act was to replace the ad hoc disaster assistance programs with an expanded crop insurance program. Although farmer participation has increased rapidly, the expected goals of the 1980 Act have not been reached and the costs have increased beyond expectation.

The adoption of this plan will:

1. **Increase the farmers participation.**
2. **Drastically reduce the administrative oosts of crop insurance.**
3. **Standardize and reduce loss adjusting ratios and costs.**
4. **Eliminate any future need for ad hoc disaster programs.**

EXHIBIT A
PAGE 1 OF 2

PROJECTED SAVINGS IN ADMINISTRATIVE COSTS IF "GENERAL AGENT SALES AND SERVICE CONTRACT" WERE USED IN THE FUTURE.

Costs based on existing contracts in force with Agency Sales and Service Contractors and Reinsurance Companies to include FCIC administrative costs. Using an estimated total of $880 million in base premium for 1990 the following analogy yields significant savings to the taxpayer.

EXISTING DUAL - DELIVERY SYSTEM

	BASE PREMIUM	EXPENSES
- AGENCY SALES & SERVICE CONTRACTOR (21% COMMISSION)	$80,000,000	$16,800,000
- REINSURANCE CONTRACT (37% COMMISSION)	$800,000,000	$296,000,000
- FCIC ADMINISTRATIVE EXPENSE		$57,000,000
EXPENSES BASED ON 1987 ANNUAL REPORT		$369,800,000

PROPOSED "GENERAL AGENT SALES & SERVICE CONTRACT"

- GENERAL AGENT SALES & SERVICE CONTRACT, $880 MILLION X 21% COMMISSION	$185,000,000
- FCIC ADMINISTRATIVE COST	$57,000,000
- FCIC LOSS ADJUSTMENT, $880 MILLION X 4%	$35,000,000
- COMPLIANCE AND OVERSIGHT, $880 MILLION X 2%	$17,600,000
- TRAINING AND CERTIFICATION OF AGENTS AND ADJUSTERS	$880,000
	$295,480,000

PROJECTED $74,000,000 SAVINGS FOR THE 1990 CROP YEAR

Projected savings could be further increased if the FCIC Corporate structure was appropriately reorganized and the APH Program was voluntary to reduce compliance and oversight cost.

EXHIBIT A
PAGE 2 OF 2

PROJECTED SAVINGS IN ADMINISTRATIVE COSTS IF "GENERAL AGENT SALES AND SERVICE CONTRACT" HAD BEEN UTILIZED FOR CROP YEAR 1987 AND CROP YEAR 1988.

1987 EXISTING DUAL - DELIVERY SYSTEM

	BASE PREMIUM	EXPENSES
- AGENCY SALES & SERVICE CONTRACTOR (21% COMMISSION)	$60,000,000	$12,600,000
- REINSURANCE CONTRACT (37% COMMISSION)	$304,000,000	$112,480,000
- FCIC ADMINISTRATIVE EXPENSE		$57,000,000
EXPENSES BASED ON 1987 ANNUAL REPORT		$182,080,000

1987 PROPOSED "GENERAL AGENT SALES & SERVICE CONRACT"

- GENERAL AGENT SALES & SERVICE CONTRACT, $364 MILLION X 21% COMMISSION	$76,440,000
- FCIC ADMINISTRATIVE COST	$57,000,000
- FCIC LOSS ADJUSTMENT, $364 MILLION X 4%	$13,560,000
- COMPLIANCE AND OVERSIGHT, $364 MILLION X 2%	$7,280,000
- TRAINING AND CERTIFICATION OF AGENTS AND ADJUSTERS	$880,000
	$155,160,000

PROJECTED $26,920,000 SAVINGS FOR THE 1987 CROP YEAR

1988 EXISTING DUAL - DELIVERY SYSTEM

	BASE PREMIUM	EXPENSES
- AGENCY SALES & SERVICE CONTRACTOR (21% COMMISSION)	$63,000,000	$13,230,000
- REINSURANCE CONTRACT (37% COMMISSION)	$373,000,000	$152,010,000
- FCIC ADMINISTRATIVE EXPENSE		$57,000,000
EXPENSES BASED ON 1987 ANNUAL REPORT		$220,240,000

1988 PROPOSED "GENERAL AGENT SALES & SERVICE CONTRACT"

GENERAL AGENT SALES & SERVICE CONTRACT $436 MILLION X 21%	$91,560,000
- FCIC ADMINISTRATIVE COST	$57,000,000
- FCIC LOSS ADJUSTMENT, $436 MILLION X 4%	$17,440,000
- COMPLIANCE AND OVERSIGHT, $436 MILLION X 2%	$8,720,000
- TRAINING AND CERTIFICATION OF AGENTS AND ADJUSTERS	$880,000
	$175,600,000

PROJECTED $46,640,000 SAVINGS FOR THE 1988 CROP YEAR

EXHIBIT B

FEDERAL CROP INSURANCE ADVISORY COMMITTEE.

(A) The Committee. The Secretary shall appoint a committee of 25 persons to be known as the Federal Crop Insurance Advisory Committee. The Committee shall advise the Congress, Secretary, and the Board of Directors of the Corporation on matters related to crop insurance.

(B) Membership of the Committee. The 25 voting members of the Committee shall be the Manager of the Federal Crop Insurance Corporation and 24 other members who shall be appointed by the Secretary, as follows:

(a) 6 individuals who will represent the views of the present companies (or managing general agencies which write crop insurance through other companies) that --

(1) have a 1989 reinsurance agreement under the Federal Crop Insurance Act.

(b) 1 of whom will represent the views of the companies writing crop insurance whose primary business is the writing of crop insurance for losses due to hail.

(c) 3 individuals who will represent the views of agencies selling non-reinsured Federal Crop Insurance.

(d) 2 individuals who will represent the views of national organizations of insurance agents or crop insurance agents.

(e) 1 individual who will represent the views of the largest national association representing wheat producers.

(f) 1 individual who will represent the views of the largest national association representing corn producers.

(g) 1 individual who will represent the views of the largest national association representing cotton producers.

(h) 1 individual who will represent the views of the largest national association representing the soybean producers.

(i) 3 individuals who will represent the views of the 3 largest national general farm organizations.

(j) 3 individuals who will represent the views of producers of fruits, vegetables, specialty crops, and other crops not specified in subparagraph (e), (f), (g), or (h).

(k) 3 individuals employed by FCIC at Management level (Assistant Manager).

(C) Co-Chairman of the Advisory Board could be chosen in the same manner as the present Commission to Improve Crop Insurance was selected.

EXHIBIT C
PAGE 1 OF 3

REINSURANCE COMPANY EXPERIENCE WITH THE RISK-SHARING PROVISIONS 1981 - 1988 WITH A GAIN OF $20,941,968

	GAIN/LOSS	LOSS RATIO	TOTAL PREMIUM
1981	287,772	1.08	12,800,000
1982	2,557,518	1.34	78,000,000
1983	(2,341,269)	2.04	107,300,000
1984	(355,621)	1.47	260,200,000
1985	3,217,551	1.55	314,100,000
1986	8,096,783	1.62	306,500,000
1987	16,454,875	1.01	303,900,000
1988	(6,975,641)	2.41	373,682,555
	20,941,968		1,756,482,555
8 YEAR AVERAGE	2,617,746	1.57	219,560,250

In 1988 with a loss of $905,906,286 only a $6,995,641 loss to Reinsurance Company or a .0077% loss (less that 1%). In 1987 an underwriting gain of almost $17 million with a 100% loss ratio.

EXHIBIT C
PAGE 2 OF 3

COMPARISON OF LOSS RATIO OF REINSURANCE COMPANIES AND FCIC (DATA OBTAINED FROM FCIC - GAO RECORDS)

TOTAL BOOK OF BUSINESS

REINSURANCE

	1988	1987
Gross Premium	373,682,554	304,145,734
Gross Losses	905,906,286	303,197,588
Loss Ratio	242.43	99.69
Gain or (Loss) Underwriting	(6,975,641)	16,901,578

FCIC

	1988	1987
Gross Premium	63,964,582	60,569,000
Gross Losses	161,512,274	64,370,000
Loss Ratio	252.50	106.21
Gain or (Loss) Underwriting	-0-	-0-

REINSURANCE ONLY

PREMIUM RETAINED

	1988	1987
Gross Premium	194,829,689	173,787,071
Gross Losses	198,441,153	110,643,780
Loss Ratio	101.85	63.67

* PREMIUM CEDED TO FCIC

	1988	1987
Gross Premium	178,852,865	130,358,663
Gross Losses	707,465,133	192,643,780
Loss Ratio	395.55	147.71

EXHIBIT C
PAGE 3 OF 3

USING FCIC LOSS RATIO ON BUSINESS CEDED BACK IN FCIC

	FCIC LOSS RATIO	GROSS LOSS PAID	USING FCIC LOSSES	SAVINGS
1988 -	252.50	707,465,133	450,709,219	256,675,914
1987 -	106.21	192,643,780	138,453,230	54,190,550

If FCIC Loss Ratio were used and no reinsurance agreement were in effect the total savings would be major. 11/20/87 GAO Report, 31% of loss should not have been paid, which may have some bearing on higher loss ratio on premium ceded to FCIC.

Savings on losses paid in 1988 -	$256,675,914
Savings on losses paid in 1987 -	$54,190,550
TOTAL -	$310,866,464

* A company may cede back to FCI all liability and they do not share in any risks.

Following are savings that could have achieved in 1987 and 1988 had this Plan for the Improvement of the Federal Crop Insurance Program been utilized:

1. Expense Savings	1987 -	$26,920,000
	1988 -	$46,640,000
	Total -	$73,560,000
2. Underwriting Gain	1987 -	$16,454,875
	1988 -	($6,975,641)
	Total -	$9,479,234
3. Gain in Losses paid using overall Loss Ration (Exhibit C Page 2 of 2)		$310,866,464

Total savings for 1987 and 1988. 1 + 2 + 3 = Total - $393,905,698

EXHIBIT D
PAGE 1 OF 2

SUGGESTED DOLLAR GUARANTEE PLAN

Cost of production protection could be offered on a dollar basis up to an amount not to exceed target price on program crops or similarly established price on other crops times the production guarantee based on the APH yield. ASCS established yields could be used as an optional method for determining production guarantee if they are factored to reflect actuarial soundness. This suggested dollar guantee plan should be a very simple program and it would utilize the present County Rate and Coverage Table.

EXAMPLE: Williams county North Dakota
Crop: Wheat
Target Price: $4.00 / bu.
APH Yield: 24 bu. / acre

75% Level:

24 bu. APH x 75% Level = 18 bu. / acre guarantee

18 bu. / acre guarantee x $4.00 Target Price = $72.00

The subsidized premium for $72.00 with 75% Level coverage per acre = $4.90

65% Level:

24 bu. APH x 65% Level = 15.6 bu. / acre guarantee

15.6 bu. / acre guarantee x $4.00 Target Price = $62.40

The subsidized premium for $62.40 with 65% Level coverage per acre = $2.31

EXAMPLE: Marshall County Minnesota
Crop: Corn
Target Price: $2.75 / bu.
APH Yield: 60 bu. / acre

75% Level:

60 bu. APH x 75% Level = 45 bu. / acre guarantee

45 bu. / acre gurantee x $2.75 Target Price = $123.75

The subsidized premium for $123.75 with 75% Level coverage per ace = $16.28

EXHIBIT D
PAGE 2 OF 2

65% Level:

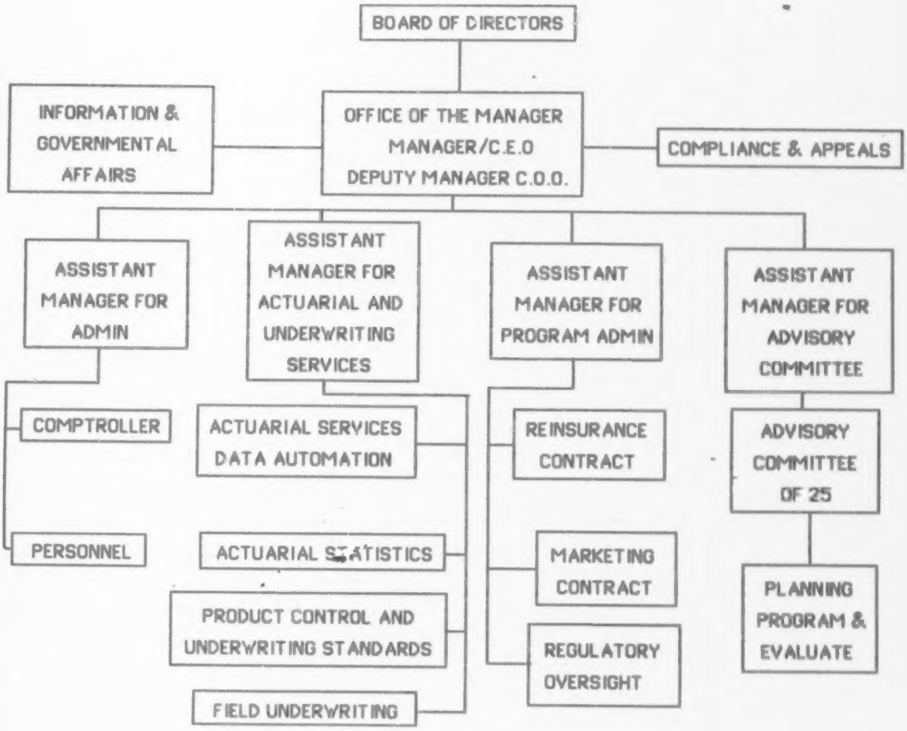
60 Bu. APH x 65% Level = 39 bu. / acre guarantee

39 bu. / acre guarantee x $2.75 Target Price = $107.25

The subsidized premium for $107.25 with 65% Level coverage per acre = $7.72

The subsidy toward premium on the 75% Level should be increased to 30%, the same as the 65% Level. Please note the difference in subsidized premium between the 65% Level and the 75% Level. This drastic premium increase for the 75% Level discourages participation on the higher level of production guarantee.

EXHIBIT E


BOARD OF DIRECTORS
INFORMATION & GOVERNMENTAL AFFAIRS
OFFICE OF THE MANAGER
MANAGER/C.E.O
DEPUTY MANAGER C.O.O.
COMPLIANCE & APPEALS
ASSISTANT MANAGER FOR ADMIN
ASSISTANT MANAGER FOR ACTUARIAL AND UNDERWRITING SERVICES
ASSISTANT MANAGER FOR PROGRAM ADMIN
ASSISTANT MANAGER FOR ADVISORY COMMITTEE
COMPTROLLER
PERSONNEL
ACTUARIAL SERVICES DATA AUTOMATION
ACTUARIAL STATISTICS
PRODUCT CONTROL AND UNDERWRITING STANDARDS
FIELD UNDERWRITING
REINSURANCE CONTRACT
MARKETING CONTRACT
REGULATORY OVERSIGHT
ADVISORY COMMITTEE OF 25
PLANNING PROGRAM & EVALUATE

ASSOCIATION MEMBERSHIP

The Master Marketer's Association of America is a not for profit association of Agency Sales and Service Contractors who sell and service Federal Crop Insurance paper. The Association promotes the preservation and expansion of the crop insurance program through public information and educational activities and by providing technical assistance and information to the appropriate governmental bodies.

Cal-Ag Ins. Services, Inc.
1601 Exposition Blvd.
P.O. Box 13428
Sacramento, CA 95813-3428

Crop Insurance Agcy. Inc.
1201 E. Church St.
Booneville, MS 38829

Farm Risk Mgrmt. Specialists
P.O. Box 88
106 N. Delaware
Butler, MO 64730

Farmers All Risk Crop Ins.
4412 74th St. #C102
Lubbock, TX 79424-2308

Federal Crop Company
758 Second St.
Chappell, NE 69129

Fred S. James - Naples
720 Goodlette Rd.
C.S. Box 413003
Naples, FL 33941-3003

Maine Mutual Fire Ins.
P.O. Box 729
44 Maysville St.
Presque Isle, Me 04769-0729

National Crop Protection
114 Single Dr.
N. Syracuse, NY 13212

Northern Crop Ins. Inc.
20 East 2nd St.
Drawer C
Williston, ND 58801

Shelby Crop Ins. Corp.
RR 9 Box 132A
Greensburg, IN 47240

Southwest Crop Ins. Agcy.
P.O. Box 225
Honey Grove, TX 75446

United Agents Crop Ins.
P.O. Drawer 208
831 Scott Ave.
Lambert, MS 38643

STATEMENT OF GEORGE F. VOHS

Submitted to the Senate Committee on Agriculture
Sub-Committee on Agricultural Production
And Stabilization of Prices

March 6, 1990

Mr. Chairman and Members of the Committee:

My name is George F. Vohs. I am the president of LongView Insurance Companies headquartered at Greeley, Weld County, Colorado. Weld county is about the 4th largest agricultural county in the United States in terms of farm production.

We operate insurance offices in Colorado, Nebraska, South Dakota and Montana. In addition, we represent some 400 crop insurance agents throughout a 36-state territory who make their principal living through the sale and servicing of crop insurance. We also represent some 15,000 farmers who continue to protect their crops, their farms, and their livelihoods by purchasing and using Federal Crop Insurance.

I don't pretend to know all the answers to the agricultural crisis, Mr. Chairman, but I do know crop insurance. I've spent the past 25 years directly involved with crop insurance as a salesman, as a Federal employee, as president of my own crop insurance company, and as a member of the Commission for the Improvement of the Crop Insurance Program.

When Congress enacted the Crop Insurance Act of 1980, which liberalized the crop insurance program and provided the private sector an opportunity to sell and service crop insurance, I was on the front line of that legislation as the director of legislation and public affairs for the Federal Crop Insurance Corporation (FCIC).

I, like everyone else, envisioned that if the Federal government could couple its resources with the sales abilities of the private sector, the crop insurance program would really "take off" and solve the problems of the then multiple ad hoc disaster programs. I even helped organize training classes to help train FCIC employees on how to cummunicate with their private sector counterparts in helping with the transition of this program.

During those sessions I distinctly remember the then editor of The Farm Journal magazine, Mr. Lane Palmer, telling us he would bet the new crop insurance program would end up like the Urban Renewal program–filled with empty houses nobody wanted to buy and a few people making a lot of money at the expense of the government.

The parallel in crop insurance isn't exactly like that today. Unlike urban renewal, the problems with today's crop insurance program are well documented. And, the Administration has now seen fit to recommend an end to crop insurance and has placed the entire problem in the hands of Congress.

Ironically enough, just before I came to this session, I received a copy of the new USDA Yearbook, entitled "Farm Management: How To Achieve Your Farm Business Goals." On page 153 is a paragraph on crop insurance as a risk management strategy which closes in this manner:

> "With the potential decline of federally financed disaster payments, crop insurance may become more important as a risk management tool."

Mr. Chairman I would like also to inject, among all the other crop insurance documentation this Committee has received, some facts that I feel are important for this Committee to consider in regard to keeping a crop insurance program.

The LongView Companies increased its servicing of crop insurance policies in 1989 by 52% compared to 1988. We went from about $8 million in premiums to more than $13 million in premiums. As you can see we aren't the largest company in the crop insurance business. And, we attribute some of the increase, but not all, to the requirement for producers to have crop insurance in order to be eligible for disaster payments.

However, computers being the wonderful instrument they are, I researched our 15,000 policies and found that, despite the big influx in 1989, the average life of our policies is 5.07 years. I further found that in our own offices, the average life of a crop insurance policy varies from 5.50 years to 12.07 years. These policies, Mr. Chairman, are written in the heartland of the farm belt.

This means to me that a large core of farmers in this country have been using crop insurance as their "safety net" and have not been relying on ad hoc disaster assistance.

When I first began in crop insurance in 1965, a farm producer could insure his crops by signing a fairly simple application and then filing an acreage report when he planted his crops. You can look back in contract file after contract file over the years and find the original application and one document each year for reporting acreage.

Contrast that to today's complex crop insurance program. Not only do you have an application, but you have multiple Actual Production History forms, you have compliance forms for wetland provisions, you have option forms for sileage, late planting, fresh apples, etc. You have ASCS forms verifying production and you have multiple policy changes, program changes, etc. Some time ago, before a Committee on Appropriations, we introduced a stack of more than 200 forms it took to write crop insurance on a single Weld County farm.

We used to go out to a farm with an application blank and a piece of paper and assist the producer in "putting a pencil" to the crop insurance program. We would come away with the sale usually in less than one hour.

Under today's selling requirements an agent has to go to ASCS for production records, has to complete multiple forms, has to have a computer to make all the necessary pricing calculations, and has to make at least two personal visits with the producer in order to adequately complete a sale.

Certainly one of the problems with today's crop insurance is its complexity.

As a member of the Commission for the Improvement of the Crop Insurance program I, along with the other members, have heard a variety of suggestions on how to improve the program. Most of them are equally as complex as the present program. And, some of them are more expensive to administer than the present program.

In my visits with farmers as a member of the Commission and as a company manager, I believe it's time to return this program to its basics. Therefore, I would make the following recommendations to this panel:

1. Eliminate price elections and coverage levels. Instead, develop insurance guarantees based upon the "value of the crop" similar to hail and fire guarantees developed by private insurers. The established production multiplied by an established commodity price would determine the maximum value of the crop. Producers could then elect to insure for full value or for any portion of the crop value with premium rates established on a per $100 of crop value. Deductibles, similar to hail coverages, could be used to prevent over insuring; however, in the long run I feel premium costs would likely determine what value a producer elected to insure. A system of "experience rating" could be used to control any continuing moral hazard (over insuring) for program users. The plan would require:

a. Establishment of a 3-year production base for each year either through producer certification, ASCS base yield records for program crops, or determined yields based upon county averages;

b. Establishment of an annual price value for each commodity which could be varied depending upon the section of the country, the futures market for a specified period, or historical information; and

c. Determination of an actuarially sound premium rate for each $100 worth of crop protection to be insured.

2. Allow the insurance to be sold any time of the year. Instead of having cumbersome sales closing dates, planting dates, etc., allow the insurance to be sold at any time during the growing season with a 10-day minimum delay period based upon crop inspection and prevailing good weather conditions.

3. Allow crop appraisals and claims adjustments to be settled at any time a loss occurs. Crop insurance has either required, or strongly suggested, that producers carry their crops to harvest before settling a claim. This is nonproductive. Producers should be allowed to make a claim, just like any other insurance, and receive an on-the-spot settlement based upon a crop appraisal. Damage appraisal methods for most crops today are sufficiently advanced to allow this determination.

4. Insure crops on the basis of each field. Remove the unit restrictions under the current crop insurance program and collect premiums and pay losses on the basis of individual fields.

5. Maintain a central bank of experience loss statistics. Some centralized data file will be necessary in order to prevent abuse of the program by producers "hopping" from one insurer to another to avoid applied premium rates based on loss experience.

While these aren't all of the changes needed to streamline and make the crop insurance program effective, these five certainly would provide increased incentive for farmers to participate in a cost-shared insurance program. It would allow producers to purchase all the insurance they felt they could afford and the options to protect their crops at optimum levels for their own purposes.

In closing, I would ask the Committee to consider that crop insurance still is a "make sense" answer to disaster protection for the American farmer. That this Committee should be aware there are some relatively simple ways to administer and control the crop insurance program and at the same time make it possible for producers to "put a pencil to it" and make a choice to insure or not to insure. These things can be accomplished regardless of who administers the program.

Finally, I would ask the Committee not to forget the thousands of farmers who have been active in the crop insurance program for years and years and have not relied on disaster relief to bail them out in emergencies. These people are proud to have "paid their way" in this program and certainly deserve a larger consideration than those producers who rely only of the political atmosphere to protect them.

Thank you Mr. Chairman. I would be happy to answer any questions.

-30-

Rules and Regulations

Federal Register
Vol. 55, No. 40
Wednesday, February 28, 1990

DEPARTMENT OF AGRICULTURE

Federal Crop Insurance Corporation

7 CFR Part 401

[Amdt. No. 58; Doc. No. 7867S]

General Crop Insurance Regulations

AGENCY: Federal Crop Insurance Corporation, USDA.

ACTION: Interim rule.

SUMMARY: The Federal Crop Insurance Corporation (FCIC) hereby amends the General Crop Insurance Regulations (7 CFR part 401), effective for the 1991 and succeeding crop years, by adding a mandatory amendment to the General Crop Insurance Policy. The intended effect of this rule is to provide that, notwithstanding the terms of the crop insurance policy and any contract for crop insurance, coverage under the terms of such endorsements will be effective subject to the availability of appropriations for the 1991 and subsequent crop years.

DATES: This interim rule is effective on February 28, 1990. Written comments, data, and opinions on this interim rule must be submitted not later than April 30, 1990, to be sure of consideration.

ADDRESSES: Written comments on this proposed rule should be sent to Peter F. Cole, Office of the Manager, Federal Crop Insurance Corporation, Room 4090, South Building, U.S. Department of Agriculture, Washington, DC, 20250.

FOR FURTHER INFORMATION CONTACT: Peter F. Cole, Secretary, Federal Crop Insurance Corporation, U.S. Department of Agriculture, Washington, DC, 20250, telephone (202) 447-3325.

SUPPLEMENTARY INFORMATION: This action has been reviewed under USDA procedures established by Departmental Regulation 1512-1. This action does not constitute a review as to the need, currency, clarity, and effectiveness of the regulations affected by this rule under those procedures. The sunset review date established for those regulations is contained in each regulation.

John Marshall, Manager, FCIC, (1) Has determined that this action is not a major rule as defined by Executive Order 12291 because it will not result in: (a) An annual effect on the economy of $100 million or more; (b) major increases in costs or prices for consumers, individual industries, federal, State, or local governments, or a geographical region; or (c) significant adverse effects on competition, employment, investment, productivity, innovation, or the ability of U.S.-based enterprises to compete with foreign-based enterprises in domestic or export markets; and (2) certifies that this action will not increase the federal paperwork burden for individuals, small businesses, and other persons and will not have a significant economic impact on a substantial number of small entities.

This action is exempt from the provisions of the Regulatory Flexibility Act; therefore, no Regulatory Flexibility Analysis was prepared.

This program is listed in the Catalog of Federal Domestic Assistance under No. 10.450.

This program is not subject to the provisions of Executive Order 12372 which requires intergovernmental consultation with State and local officials. See the Notice related to 7 CFR part 3015, subpart V, published at 48 FR 29115, June 24, 1983.

This action is not expected to have any significant impact on the quality of the human environment, health, and safety. Therefore, neither an Environmental Assessment nor an Environmental Impact Statement is needed.

FCIC herewith amends the General Crop Insurance Regulations (7 CFR part 401) to provide a mandatory amendment to the provisions for coverage therein to provide that, notwithstanding the terms of the General Crop Policy, coverage will be effective subject to the availability of appropriations for the 1991 and subsequent crop years.

The President's budget for 1991 provides for the elimination of the Federal Crop Insurance program by not funding the program for the 1991 crop year. In view of the uncertainty of Congressional action on that budget proposal, FCIC believes it is necessary to publish a rule requiring an endorsement on all policies restating the general rule that public programs are subject to the availability of funds, so as to put all parties on notice that insurance coverage may not be available for the 1991 crop year. Equitable principles dictate that all parties concerned be aware of the uncertainty of insurance for the 1991 crop year.

Since Texas Citrus Tree insurance requires that contract changes be on file by February 28, an emergency situation exists requiring that this rule be published, effective in less than 30 days without prior notice and comment.

This rule is effective on February 28, 1990. FCIC is soliciting public comment on this proposed rule for 60 days following publication in the **Federal Register**. Written comment should be sent to Peter F. Cole, Office of the Manager, Federal Crop Insurance Corporation, Room 4090, South Building, U.S. Department of Agriculture, Washington, DC 20250.

All written comments received pursuant to this proposed rule will be available for public inspection and copying in the Office of the Manager, Federal Crop Insurance Corporation, Room 4090, South Building, U.S. Department of Agriculture, Washington, DC 20250, during regular business hours, Monday through Friday.

This rule will be scheduled for review so that any amendment made necessary by public comment will be published in the **Federal Register** as quickly as possible.

List of Subjects in 7 CFR Part 401

Crop insurance.

Interim Rule

Accordingly, pursuant to the authority contained in the Federal Crop Insurance Act, as amended (7 U.S.C. 1501 *et seq.*), the Federal Crop Insurance Corporation hereby amends the provisions of the General Crop Insurance Regulations (7 CFR Part 401), effective for the 1990 and succeeding crop years on any existing carryover contract or new contract for the 1991 crop year, by adding a mandatory amendment to the provisions for coverage therein, effective for the 1991 and succeeding crop years, as follows:

PART 401—[AMENDED]

1. The authority citation for 7 CFR part 401 continues to read as follows:

Authority: 7 U.S.C. 1506, 1516.

2. 7 CFR 401.8 of the General Crop Insurance Regulations is amended by adding a new paragraph (e) at the end thereof to read as follows:

§ 401.8 The application and policy.

* * * * *

(e) Notwithstanding the terms of the crop insurance endorsement and any contract for crop insurance under the provisions of this part, coverage under the terms of such crop insurance endorsement will be effective subject to the availability of appropriations.

Done in Washington, DC on February 21, 1990.

John Marshall,

Manager, Federal Crop Insurance Corporation.

[FR Doc. 90-4725 Filed 2-27-90; 8:45 am]

BILLING CODE 3410-08-M

Senator **Pryor**. And if there are no further comments from our panelists—yes, sir? Please, Mr. Gibson.

Mr. **Gibson**. Just one final comment. The FCIC and private industry did put together a task force to study the soybean situation in the Southeast, and they did come forward with recommendations. I think that industry and FCIC for the most part said that those recommendations would solve many of the participation problems in the Southeast in soybeans, but that proposal has been rejected out of hand. So you might take an opportunity to look at that.

Senator **Pryor**. Well, as you can see, we have not gotten our letter answered yet. We hope to get that. Ladies and gentlemen, I thank all of you very much. Our meeting is adjourned.

[Whereupon, at 5:25 p.m., the subcommittee recessed, to reconvene at 2:15 p.m., Thursday, March 8, 1990, in room SR-332, Russell Senate Office Building.]

PREPARATION FOR THE 1990 FARM BILL

Wheat

THURSDAY, MARCH 8, 1990

U.S. SENATE,
SUBCOMMITTEE ON AGRICULTURAL PRODUCTION AND
STABILIZATION OF PRICES OF THE
COMMITTEE ON AGRICULTURE, NUTRITION, AND FORESTRY,
Washington, DC.

The subcommittee met, pursuant to notice, at 2:15 p.m., in room SR-332, Russell Senate Office Building, Hon. David H. Pryor (chairman of the subcommittee), Hon. David L. Boren, presiding.

Present or submitting a statement: Senators Boren, Conrad, Daschle, Baucus, Kerrey, Dole, Cochran, Boschwitz, Bond, and Gorton.

Also submitting a statement: Senator James A. McClure.

STATEMENT OF HON. DAVID L. BOREN, A U.S. SENATOR FROM OKLAHOMA

Senator BOREN. I think we will go ahead and commence. There are some other members who will be arriving for the hearing.

The subcommittee hearing this afternoon is to examine the part of the farm bill that has the most direct impact on the economy of my State, and I know the economy of several of the States represented with Senators who have planned to attend this afternoon, and that is the wheat program. I think our witness panels will really make a great contribution today and I thank them for joining us.

I would also especially like to thank Senator Pryor of Arkansas, chairman of the subcommittee, for allowing us to meet and to go forward with this study today.

In general, I believe the mechanics of the current wheat program are sound. The target price/deficiency payment system, combined with strong export programs, has allowed the United States to regain some of the wheat markets we had lost in the past without completely sacrificing farm income.

While it doesn't include many changes in the wheat program itself, the administration's farm bill proposal does propose a sweeping flexibility plan and a significant change in reserve policy, both of which would significantly affect the entire wheat industry. Therefore, I believe that we should review these proposals very, very carefully, and that is the principal purpose for our being here today.

I have some specific concerns about the administration's total farm base proposal, as well as the implementation of current law that I think we should address today.

First, the administration's total farm base proposal obviously addresses the problem of rigid farm programs. I certainly agree with this goal, and for a long time I, along with other members of this committee, have advocated a more flexible farm program leaving more decisions to the farmers. This farm bill presents us with a great opportunity to move in the needed direction.

At the same time, however, the Agriculture Committees cannot operate in a vacuum. The U.S. Department of Agriculture is obviously the best equipped institution to inform the committees of projected changes in cropping patterns and farm income that would occur under its plan. Wheat farmers and their Senators from those States want to know how the industry will be affected, what shifts do we expect in planting patterns if we adopt this total farm based proposal.

The USDA farm bill was released a month ago, but the Department has been less than forthcoming with the assumptions upon which the plan is based. Preliminary jockeying should now come to an end and the Department should use its expertise constructively by working with the committee to forge a better farm bill.

It is extremely important that we know the administration's assumptions, the Department's assumptions, about what will happen with patterns. There are parts of my State, for example, because of climate and other conditions, that farmers simply do not have the option to shift to other crops, and we have to do a lot of thinking about what will happen in other areas of the country where people might be able to shift from, let us say, corn to wheat, or areas of the country where we have double cropping or triple cropping, and whether or not those people will end up going into wheat and what that will do to markets, what are the assumptions.

Second, I am concerned about the administration's use of the Findley authority that allows the Secretary to lower the loan rate by an additional 20 percent from the base loan rate if he deems it necessary to maintain U.S. competitiveness in world wheat markets. I have always believed that the concept has merit and should be used in certain situations, but I cannot help but wonder if the Department has used this discretion carelessly. I am not sure how lowering the loan rate from $2.44 to $1.95 helps our competitiveness when the projected wheat price is $3.20, for example.

Like it or not, nonrecourse loans have traditionally been used by many producers as interim financing while they market their wheat. The Department should not use this discretion lightly, especially when its effect on our competitiveness is questionable.

So while this is in the law, while I certainly don't oppose it being in the law, how it is administered is very, very important. And if we lower it at a time when it has no impact on competitiveness, we may end up hurting the ability of some of our farmers to get financing in the interim. So this is something else that I hope we will address today as we hear from our witnesses.

I will pursue these and other topics important to the wheat industry as we hear from our witnesses today.

We have some excellent witnesses, as I say, to give us some background on these and other issues dealing with the wheat program.

I am very pleased so many of our colleagues are here. I know Senator Baucus is handling the Clean Air Act legislation on the floor and has other responsibilities. I will turn to him for any opening comments he might like to make.

STATEMENT OF HON. MAX BAUCUS, A U.S. SENATOR FROM MONTANA

Senator BAUCUS. Thank you very much, Mr. Chairman. I would be here for the entire hearing but for the Clean Air Act now on the floor which I am managing—I must be there to try to get Senators to come to the floor and offer amendments. This Clean Air Act, frankly, Mr. Chairman, reminds me of an experience of mine in the first month of September. We in Montana celebrated our 100th anniversary, our centennial, with a cattle drive. And when the cattle drive began—we had about 3,000 head of cattle—they were all scattered in all directions and running, you couldn't control them, and it took about 4 or 5 days for the cattle to become trail broken so we could handle them pretty well.

Senator BOREN. And we are the cattle?

Senator BAUCUS. I am saying, Mr. Chairman, it does remind me of the cattle drive. I won't take the analogy any further, but it does remind me of this cattle drive.

Senator BOREN. I have a few little amendments that would help a few of the cattle get in line that I might talk to you about.

Senator BAUCUS. Mr. Chairman, I thank you for allowing me to proceed.

As this subcommittee considers the wheat program in the 1990 farm bill, Mr. Chairman, I think we should be working toward two principal goals: First, increasing wheat producers' income, and second, expanding wheat exports.

Generally, I think the 1985 farm bill has served wheat producers fairly well. The bill did help protect farm income and boost exports.

But the 1985 farm bill was written for the conditions that existed in 1985.

In 1990, I think we must write a farm bill that responds to the challenges we face in 1990 and beyond.

We should keep what is good from the 1985 farm bill, but there are many areas that need improvement.

TARGET PRICES

The most important change that we must make in the 1990 farm bill is ending the steady decline in farm target prices.

While target prices have been going down, farmers' costs have been going up.

One of my top priorities in drafting the farm bill will be incorporating reasonable cost of living adjustments into target prices.

I am going to introduce a bill to do this when the Congress reconvenes after the recess.[11]

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[11] S. 2336, Target Price Adjustment Act of 1990, introduced Mar. 26, 1990. Some provisions included in S. 2830, Food, Agriculture, Conservation, and Trade Act of 1990.

Target price increases are overdue. In the European Community, the wheat target price is over $7 per bushel. In the United States, it is barely $4.

I often hear my urban colleagues complaining about the high cost of the farm program, but frankly, that criticism is out of date.

The farm program did cost $26 billion in 1986. But in 1989, the farm program cost the U.S. Government somewhere between $10 and $12 billion.

In other words, the cost of the farm program has been more than cut in half in 3 years.

The farm program is now the fastest shrinking major item in the Federal budget.

TRADE PROGRAMS

One of the most successful portions of the 1985 farm bill was the international trade title.

In Montana, we depend heavily on export sales. We exported about 85 percent of our wheat crop last year.

The Export Enhancement Program (EEP) has worked better than we could have hoped. For example, in 1985, before the use of the Export Enhancement Program began, the United States held only 25 percent of the world wheat market. In 1988, after 3 years of the Export Enhancement Program, the U.S. share of the world wheat market was up to 50 percent. From 25 percent to 50 percent in just 3 years.

The Targeted Export Assistance (TEA) Program has been another major success.

Unfortunately, the Reagan administration, and now the Bush administration, have consistently cut the Export Enhancement Program and the Targeted Export Assistance Program. The administration has also failed to use all the funds Congress authorized for those programs.

Now the administration is negotiating with other nations in Geneva to cut all agricultural support programs.

Our Nation's farm program must also not be considered in isolation. We must consider it in a context of world agricultural trade. We should negotiate with other nations in Geneva to cut all agricultural support programs.

Perhaps if all nations mutually cut subsidies at once, it would benefit the United States.

But we Americans cannot do it alone, and I will vehemently oppose any unilateral cuts in U.S. export programs.

These trade programs work and they must continue. We cannot let trade negotiators in Geneva write the 1990 farm bill.

The 1990 farm bill will ultimately be written by the U.S. Congress, Mr. Chairman, not by our trade negotiators.

I have already introduced legislation to extend the EEP and TEA in the 1990 farm bill.

I look forward to hearing from our witnesses today on their recommendations for the wheat program.

I will keep very close tabs on this hearing because it is imperative that as we write our farm program, particularly the wheat section, we take these and other strengthening provisions into consideration.

Senator **Boren**. Thank you very much, Senator Baucus, and I think the fact that you would take time to be with us today underlines the importance you attach to this issue, because we do know the responsibilities you have, the many hours, I know, of around-the-clock meetings, virtually, in addition to handling this bill on the floor. So we know you will have to leave us, but again, I think your taking time to come over certainly underlines your interest in this whole subject.

And let me say, speaking as chairman of the Subcommittee on Domestic and Foreign Marketing and Product Promotion of the Agriculture Committee, we will proceed vigorously to mark up that section of the farm bill. We are going to do that among some of the first sections we mark up, and we are not about to wait for the trade negotiations to go forward before we mark up. I think it is important for us to send a strong signal of continuation of these export enhancement programs, and we have had several good bills introduced, several of my colleagues on this side of the aisle, Senator Cochran and I and others have introduced what we call the "Buy American Export Program," so we are ready to move forward and work on it.

Senator Gorton, any opening comments you would like to make?

STATEMENT OF HON. SLADE GORTON, A U.S. SENATOR FROM WASHINGTON

Senator **Gorton**. Mr. Chairman, I thank you particularly. You have invited me further up the table, but I am here as a guest in this subcommittee and not as a member, and I appreciate this opportunity simply to express my importance in what the subcommittee is about to do. I also want to say how encouraged I was by your opening statement. The State of Washington ranks third behind only Kansas and your own State in the total production of wheat, and we have many of the same concerns that you have.

The flexibility program, which is an integral part of this proposed farm bill, has many attractive features and a great deal of merit, but it does not have the same impact across the country. As in your State, most of our wheat and barley growers really do not have alternative crops, and most particularly, alternative program crops, to which they could shift. And they are deeply concerned that this kind of program means that in bad years, of course, they are going to be stuck with their crop, but that in good years they are not going to be able to make it up because so much more wheat will have been produced that it will depress prices even then.

And so starting from what is in general a good idea of producing for the market and with environmentally beneficial impacts, we have to consider whether or not this will have people producing for the market or simply for speculation. My own wheat association has a suggestion of a limitation of the amount or degree of other program crops which can be grown, wheat which can be grown on, basically, land which has been used for other production.

Senator **Boren**. Sort of try a pilot program of flexibility and see how much shift would occur.

Senator **Gorton**. Try a pilot program, together with no deficiency payments for those crops, allowing it to stay in the base but treating them as if they were nonprogram crops. And with your encouragement and support, and with the concern many others have here, I believe that we can meld and to try out what is a good idea, but I am convinced that we ought to do it in a way which does not unduly penalize those of our farmers, whether in Oklahoma or Washington or any other State, who really are not in a position to take advantage of it.

Much of the rest of this program meets with the approval of the growers in my State. I associate myself with your remarks and those of other Senators on the absolute imperative nature of our export enhancement programs and the need to be competitive and increasingly competitive and increasingly aggressive in overseas sales.

But I want to thank you for this opportunity to express my views this early and to say how encouraged I am to find that I am thinking of many of exactly the same things that you are.

Senator **Boren**. Thank you very much, Senator Gorton.

Senator Conrad, any opening comments that you would like to make?

STATEMENT OF HON. KENT CONRAD, A U.S. SENATOR FROM NORTH DAKOTA

Senator **Conrad**. Thank you, Mr. Chairman. As you know, I represent a major wheat producing State, and the latest USDA figures show that the prices farmers are receiving and the return that they are receiving is below production cost. No industry can survive for very long in that environment, and when I look at the testimony, the prepared testimony of Mr. Gardner, I see that we may need to reduce wheat target price from $4 to $3.80 to meet the President's budget goals.

Senator **Boschwitz**. Where does it say that?

Senator **Conrad**. Please look at page 14 for the relevant information.[12] That is unacceptable, enough is enough. My State is in exceedingly difficult financial straits. We are in the third year of drought. Everywhere I go farmers are asking me what are you going to do to strengthen income, not cut income. And a suggestion, even hypothetically, that we need to be talking about cutting target prices from $4 to $3.80 when we are already below the cost of production is a disaster. I hope with every fiber of my being, Mr. Chairman, that we are going to reject such suggestions. That just cannot be the direction that we go.

I hope we will have a chance to fully air these points as we go through the hearing, Mr. Chairman, and I thank you for holding it and for your earlier comments.

Senator **Boren**. Thank you very much. Senator Boschwitz, any opening comments?

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[12] See p. 236 for page 14 of Mr. Gardner's prepared statement.

STATEMENT OF HON. RUDY BOSCHWITZ, A U.S. SENATOR FROM MINNESOTA

Senator BOSCHWITZ. Well, I am not a member of this subcommittee either, I don't believe. I just show up at all the meetings. [Laughter.]

I was pleased to hear Senator Baucus note that our exports have gone up from the bottom 25 percent of the world wheat market to, he said now 50 percent, I think it might not be quite that high, but that is of interest to those of us who attended a hearing here the other day about grain quality standards, that apparently the buyers are buying our goods.

I certainly agree with my friend from North Dakota. One of the ways of increasing the target price is to jump right on my bill, Senator, where we don't have ARP's. You know, an ARP of not many years ago of 27.5 percent, you only get paid for what you produce on 72.5 percent of the land, yet your overhead and costs remain on the 27.5 percent that is not productive and on which you cannot grow. And all we have done is we have emboldened others around the world to increase their production.

As the Assistant Secretary notes at the very beginning of his prepared testimony, "World wheat production has more than doubled in the past three decades," and I am sure that if you trace the acreage, you will see that acreage has indeed increased as we have decreased ours and that we really have just penalized ourselves.

I am looking forward to the testimony of the witnesses, Mr. Chairman, and I am pleased to be here, whether a member of this subcommittee or not.

Senator BOREN. We are always happy to have you. In fact, I was just checking to see how many members we have on the subcommittee. I think at least initially with our initial attendance we may have broken records and had more than a 100 percent of attendance of the subcommittee in total numbers, which is a good trend to set around here. We are glad to have you.

Senator Daschle.

STATEMENT OF HON. THOMAS A. DASCHLE, A U.S. SENATOR FROM SOUTH DAKOTA

Senator DASCHLE. Mr. Chairman, I will be very brief. I commend you for your leadership in this whole area. Your statement set a proper tone, and certainly as we go through the hearing this afternoon, as well as our deliberations, I hope we remember many of the points made in your opening remarks.

My only real concern is that as we decide on policy and as we decide which tools are the most effective in implementing that policy, that we all have a better understanding than we have had in the past about what our goals are. I am not sure we even know what those goals are when it comes to wheat, or for that matter, most of our commodities today. I would hope that we could all agree upon some goals, whether specified or not, general or specific. I think it is very important that we decide before we determine what the ARP will be or whether we use EEP, or whether we have conservation reserve, or whether we do any one of a number of things that require the utilization of past tools or new ones, that we have a better understanding of where we are going, what will be our goals in wheat, both domestically and internationally, and how will we accomplish them.

And so I hope this hearing can enlighten us in that regard, and again, I reiterate my commendation to the chairman for his leadership in this effort.

Senator BOREN. Thank you very much. I think what you have said is extremely important, and what has been said by our colleagues also in terms of keeping an eye on farm income and we look at these various different tools we use. I think that is one of the things we have to keep before us, is estimating what the impact will be on farm income as we implement and use these various kinds of tools that you have talked about. So that is certainly one of the goals, I think perhaps the most important goal of all to keep our attention focused. I appreciate your comments very much.

Senator Cochran, again, it is a privilege to join you in introducing our export enhancement bill, and we would welcome any comments that you might have.

STATEMENT OF HON. THAD COCHRAN, A U.S. SENATOR FROM MISSISSIPPI

Senator COCHRAN. Thanks, Mr. Chairman. When I walked into the room somebody said, "What are you doing here, this is about wheat?"

In Mississippi we are growing more and more wheat each year. A lot of people didn't realize that maybe, but according to the 1987 Census for Agriculture, we had almost 2,000 wheat farmers in Mississippi, and they produced wheat in 1989 that has an estimated value of about $61.2 million. So it is a substantial amount of money for our State and is a very important part of our State's economy.

But beyond, that it is important I think for all of us to get an overview of all the commodity programs as we proceed to the mark up of our farm bill this year, and I am anxious to hear what the witnesses recommend that we ought to do as far as wheat is concerned in this new farm bill.

So thank you, Mr. Chairman, for being here and having these panels of witnesses arranged for us today to talk with. Thank you very much.

Senator BOREN. Thanks very much, we appreciate you joining us.

We will begin with our witnesses now, if Dr. Gardner would come forward. We have with us as our first witness Dr. Bruce Gardner, Assistant Secretary for Economics from USDA. And Dr. Gardner, we welcome you. Let me say that we will receive your full prepared statement for the record and if you would like to summarize the highlights of your statement, perhaps that would be best and then we can turn to questions and discussion from members of the committee. Thank you for joining us.

At this point in the hearing record we will receive and insert the prepared statements of Senators Dole, Bond, and McClure.

PREPARED STATEMENT OF HON. ROBERT DOLE, A U.S. SENATOR FROM KANSAS

Mr. Chairman: I would like to begin by thanking the chairman for his leadership in holding this subcommittee hearing. The chairman's home State of Oklahoma is clearly an annual leader in wheat production, and his active participation in writing the wheat title of the 1990 farm bill is welcomed and appreciated.

Being a Kansan, I share the chairman's interest in the wheat program. With the exception of the 1989 drought year, where 30 percent of our 12.4 million acres were a total loss, Kansas has maintained a prominent lead as the No. 1 wheat producing State in the Nation. Wheat production is a major force in the Kansas economy, generating revenues which flow into and sustain our rural businesses and communities. I think the farmers in Kansas would agree the 1985 farm bill has been a good program for them and for the rural economy, and it provides an excellent foundation to build from in 1990.

Perhaps the most important factor leading to the success of the wheat program, and one of the biggest success stories of the 1985 bill, has been the Export Enhancement Program (EEP). EEP has guided our way to an emerging preeminence in international agricultural trade. We have convinced the competition that we are serious about competing in the marketplace, and have gained new leverage in the current GATT negotiations. This program has allowed us to recover market share, reduce surplus stock levels, and increase both the volume and value of wheat exports. Our wheat export volume has increased by 40 percent since 1985, and in the 5 years of EEP's existence we have realized almost $10 billion in new commodity sales at a program cost of only $2.7 billion. To me, those figures spell success, and send a strong signal to this committee to continue and expand the program. Our future competitiveness depends on it.

Another key element of this year's farm bill which could have significant impact upon wheat farmers is the issue of flexibility. This is a sound concept; farmers need the opportunity to plant for the market and to follow prudent rotational practices. But I would urge the committee to approach some of the proposals with caution until we have a better grasp on what effect total or even partial flexibility will have upon shifts in program crop acreage bases. We don't want to totally throw supply management out the window and open the door to chronic surplus and depressed prices for any commodity. The American farmer needs planting flexibility, but we must be sure not to inadvertently destroy an optimal product mix by allowing major shifts in program crop acreage.

I would again like to stress that it is imperative that wheat farmers know what the 1991 wheat program will be prior to planting this fall. The past two farm bills have been signed in December, and those on this committee who hail from wheat country know that this is too late. We have a responsibility to the wheat farmer to implement the program in a timely manner, and I hope that we can fulfill that duty. If the farm bill is not completed by midsummer, I will push for a 1-year extension of the 1985 farm bill so we don't end up with our wheat growers making planting decisions on a wheat program which doesn't exist.

As we focus on the wheat program, we must keep a watchful eye upon farm income. We reached record levels in 1989, and in order to continue the trend we must make full utilization of tools such as EEP. Increased export value is a key area where we have seen an increase in farmer income through the market, and this will become increasingly important as we attempt to sustain farm income and at the same time deal with the Federal deficit.

I have been reviewing several proposals, and I look forward to working with the committee on this major commodity title of the 1990 farm bill.

PREPARED STATEMENT OF HON. CHRISTOPHER S. "KIT" BOND, A U.S. SENATOR FROM MISSOURI

Mr. Chairman, it is a pleasure to join you this afternoon to discuss yet another important Missouri commodity: wheat. As we proceed with these farm bill hearings, I am struck by all of the various commodities which are produced in Missouri. Although we are blessed to have such a diverse agricultural economy, it is proving somewhat difficult to arrive at positions which can be supported by everyone involved.

Missouri now ranks seventh nationwide in all wheat production. Our wheat production, 97 percent of which is Soft Red Winter, has been very erratic in recent years. In 1986, Missouri produced about 18 million bushels—in 1989 production rose to almost 87 million bushels. The value of the 1989 crop was more than $325 million—behind only soybeans, hay and corn.

As I have mentioned in earlier hearings, I have held several meetings throughout Missouri to learn what the producers themselves have in mind for the farm bill. In general, there is support for the provisions of the current farm bill. However, I did hear quite a bit of support for additional planting flexibility.

My producers indicate that flexibility is not only important for marketing, but also agronomic factors. Missourians will have to build 29,000 miles of terraces and use over 5 million acres of conservation tillage or no-till due to conservation compliance. There is a great need for increased flexibility to simply meet the conservation compliance requirements. I am afraid that in the absence of flexibility, and with lower income support, producers will simply opt out of Federal farm programs.

During these meetings, I heard support for the normal crop acres concept. Some producers questioned the administration's proposal to pay deficiency payments whether a crop is produced or not—yes I even heard decoupling mentioned.

Mr. Chairman, inside the beltway I have noticed somewhat of a shift on flexibility recently. Several commodity groups now seem to be calling for only limited flexibility. This fallback is especially difficult for someone representing a State with a diverse agricultural economy.

As I look for possible compromise, I am reluctant to accept only limited flexibility. I hope we have not underestimated the impacts of conservation compliance and the need for unrestricted flexibility.

Mr. Chairman, I wonder what the reaction would be to moving to a normal crop acres concept yet restrict deficiency payments to the commodity with the base. In other words, if you have a wheat base and plant winter rapeseed, you would not receive the wheat deficiency payment. This would allow flexibility without the possibility of program distortions.

Once again, I thank the Chairman for scheduling this afternoon's hearing. You have assembled a fine group of witnesses and I look forward to hearing from them.

PREPARED STATEMENT OF HON. JAMES A. MCCLURE, A U.S. SENATOR FROM IDAHO [13]

Mr. Chairman, members of the subcommittee, I thank you for allowing me to address the subcommittee and discuss what is an important issue to many of my constituents in Idaho—the renewal of the Wool Incentive Act—as a part of the 1990 farm bill. The Idaho Woolgrowers Association, which represents 1,200 sheep producers, raising 277,000 sheep, fully supports the continuation of the act as it currently stands. They voted in their convention last November to support a continuation of the act. I urge you to renew the Wool Act as a part of the 1990 farm bill legislation.

The law as it currently exists has achieved the purpose of the 1954 act, that of providing market sensitive income stability for wool and lamb producers. It has provided incentives for improving the quality of U.S. wool and has increased U.S. competitiveness in the domestic market. Although the wool promotion program has benefited most of the industry it has some weaknesses in implementation which I will discuss later, with a recommendation for improvement.

The Wool Act has provided much needed income in rural areas and helped stem the flow of agriculture workers from the rural areas to cities. Small towns and cities across America benefit from stability in wool markets which provides much needed income to rural residents. The Wool Act does all of these things without being a burden to the American taxpayer or a drain on the Treasury. Wool incentive payments to producers are taken from tariffs collected on raw wool and certain wool products entering the United States from foreign countries. Payments under the Wool Act to ranchers and farmers has used only $2.05 billion of the $4.68 billion of wool tariff dollars collected under the tariff. The rest of the funds collected have remained in the Treasury helping to reduce the huge national deficit.

Mr. Chairman, much has been written and said about the need for rural development funds to assist small towns and cities across America. I contend that we would spend less on rural development if we just allowed farmers and ranchers who are already there to grow and expand. Woolgrowers and lamb producers are already there and producing, indeed in some areas expanding. By continuing the Wool Act in its present form, you will be providing the groundwork for real rural development without spending any additional taxpayer dollars.

In the Wool Act, Congress allowed for the first promotion and market development program to be developed in an effort to increase the use and sales of wool. The law provided the first producer funded self-help program in American agriculture history. Through this program and other regional efforts consumer demand for wool and lamb have increased. Although I believe in the concept of the national wool promotion program I do have a problem with the implementation of the promotion and marketing program. Because the national program does not address regional and local problems in its education and outreach programs, and because I believe that it has become too top heavy in management, I believe that some changes need to be made in the implementation of the program.

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[13] The Subcommittee on Agricultural Production and Stabilization of Prices of the Committee on Agriculture, Nutrition, and Forestry deeply regrets that this statement, intended for the March 2, 1990, hearing on Wool and Honey, Part XII, was misplaced and will be printed as part of the March 8, 1990, Wheat hearing, Part XIII, Preparation for the 1990 Farm Bill series.

I am speaking of the need to allow statewide, regional or local use of national promotion and research funds by State or regional associations. Under section 708 of the National Wool Act of 1954 as amended, the Secretary of Agriculture is authorized to enter into agreements or approve agreements between trade associations or others engaged in handling of wool, sheep or these products for the purpose of developing promotion programs. These programs are for advertising, sales promotion, development and dissemination of information of product quality, production management and marketing of wool and sheep products.

Currently the USDA, through the Agricultural Marketing Service (AMS), has allowed only one contract for promotion, marketing, advertising and education. That contract is with the American Sheep Producers Council (ASPC). The Idaho Woolgrowers Association has for several years been unhappy with the way in which the national association spent the promotion and education funds. Western issues, such as concentration in the meat packing industry, education of the public on Federal lands issues and regional lamb promotion programs, have not received attention from the national association. Because of this the Idaho Woolgrowers Association has requested that the amount of funds sent to the national association for promotion and education under the act be returned to Idaho for use in a regional program.

The Wool Act clearly states that multiple contracts are allowed. The Idaho Sheep Council has already indicated that a promotion program would be possible in conjunction with local packing plants in areas which would benefit regional lamb producers directly. In addition, these funds would be used in consumer and producer education in concurrence with USDA approval. I have contacted USDA AMS concerning this proposal and the Assistant Secretary of Marketing and Inspection has been contacted regarding this program request. At this time the USDA has not granted the request but has had serious discussions concerning the feasibility of the request. The Idaho Sheep Council and the Idaho Woolgrowers fully support this as does the Idaho congressional delegation.

I will do everything possible to help them obtain this State program. Should this not be possible to achieve administratively, I will propose legislation which will achieve this end.

Mr. Chairman and members of the subcommittee, I certainly do appreciate the opportunity to speak before you today. I look forward to working with the committee as it continues its work toward completion of the farm bill.

STATEMENT OF BRUCE L. GARDNER, ASSISTANT SECRETARY FOR ECONOMICS, U.S. DEPARTMENT OF AGRICULTURE, WASHINGTON, DC

Mr. **Gardner**. Thank you, Mr. Chairman and members of the subcommittee. I appreciate the opportunity to appear to discuss wheat in the 1990 farm bill, and as you suggest, I will just give a few highlights of what is in the prepared testimony.

ACREAGE FLEXIBILITY

What I would like to do is say a little about a general issue that has come up several times at these hearings, namely, flexibility. Our "Green Book" proposals on flexibility have had a generally good reception, I think, but there have been expressions of dissatisfaction. Several alternative proposals have been put forth. Because this dissatisfaction has often been based on misunderstanding or dubious economics and because the alternatives to our proposals create still more problems, I believe, I would like to review a few points on this subject.

First, what is wrong that flexibility is supposed to fix? It is that current programs, despite their many virtues, provide distorted incentives for acreage allocation decisions that farmers must make.

For example, based on market expectations, suppose as a hypothetical example that sunflower seeds yield an expectation of $80 per acre in return for a farmer after taking out the nonland costs, while wheat yields $40 per acre. The farmer would normally plant sunflowers in response to this situation, but under current programs if the farmer had been planting wheat, planting sunflowers instead would have cost about $45 per acre in deficiency payments and loss of payment base for future years. So the farmer sticks with wheat and we get too much wheat planted and too little sun seeds, despite the strong market signal that the other crop is wanted.

This is not a trivial source of inefficiency. In the example I just gave an acre taken from wheat and put into sunflowers would have generated a net gain to society of $40. That is, removing obstacles in the way of acreage reallocation doubles the real return to land from $40 to $80. From the viewpoint of national output or real income generated for our farmers and our economy, a freely allocated acre is worth 2 restricted acres, but the farmer is prevented my program provisions from seeing the economics properly.

KEY VIRTUE OF OUR PROPOSAL

The key virtue of our proposal is that within the set of program crops and oilseeds, it permits acreage decisions to be made on the basis of market conditions.

SEVERAL ALTERNATIVES TO OUR PROPOSAL DO NOT HAVE THIS VIRTUE

Now, several alternatives to our proposal do not have this virtue. For example, base substitution is involved in several proposals I have heard. These proposals merely set up a chase for target prices. In the wheat/sunseed example, this approach would likely have drawn land from the $80 to the $40 use. That is, we would have flexibility, but in the wrong direction.

To take another example, elimination of cross-compliance would add to flexibility in one way. Suppose the market was signaling for more wheat. Then a farmer who had no wheat base could plant wheat on soybean land, say, and still keep corn payments. But if the farmer wanted to plant the wheat on corn base, or plant soybeans on corn base, the decision would still involve a comparison of the target price for one crop against the market price of the other. This is the situation that leads to this misallocation of the $80 versus the $40 variety.

To me the most puzzling response to our flexibility proposal is the idea that we should allow farmers to make acreage reallocations in response to market conditions, but only up to some very small amount like 10 to 20 percent of a crop's base acreage, are the kind of figures I have heard. This is like telling farmers who previously weren't allowed to use tractors that now they can use them, but only 1 day a week.

Why make such a restriction? These restrictions seem to me not a concern of farmers so much as a kind of "inside the beltway" phenomenon, an instance of the general presumption that the Government just can't let people go ahead and do what they want to do. We worry that people making choices in markets in uncertain situations will follow a kind of self-destructive herd instinct of rushing to some commodity of the moment.

But what evidence is there of this behavior among the hundreds of unregulated commodities in our economy? Very little, I would submit. Occasionally we see events like a seemingly irrational 200 point drop in the Dow Jones average, or panic selling of houses perhaps generating a price plunge, or overproduction and price declines in a vegetable crop. Such cases may sometimes reflect a herd instinct or something like this that people regret making later, but we wisely don't legislate that people can only sell 10 percent of the stock they own, or that no more than 10 percent of the houses in a town can be sold.

Limits of 10 or 20 percent on acreage flexibility make even less sense. That such limits are even seriously considered shows how off-base we have been thrown, and I think it has happened because of years of thinking of farmers' acreage as an object of governmental regulation. And our proposal, it seems to me, is a step toward market orientation in this, as in some other ways, to end that way of thinking.

Thank you, Mr. Chairman. I will respond to any questions you have.

Senator BOREN. Thank you very much, Dr. Gardner. Let me go back to the point that I was making earlier in my introductory statement. I recently held a field hearing for this committee in Enid, Oklahoma [14] where farmers certainly acknowledged the need for more flexibility. I don't think they are quarreling with the basic approach that you have been talking about in terms wanting to see greater flexibility. I know several of us on this committee have expressed a desire to see that. But we do have a situation where many of our farmers simply cannot shift, have a very, very constrained range of options.

Now, this isn't true in some parts of the country, but I am talking about in dry land wheat farming areas. For example, in the northwestern part of my State they just really don't have many options. They can't switch over to vegetables or to something else. And there is a real concern about how many acres would shift elsewhere. And as was said by Senator Gorton before he had to leave, the good years make up for the bad years, and if you have a good price all of a sudden, a good projected price, are we going to have people where they can shift in other parts of the country going in and increasing wheat production to the degree that we will even out those good years in terms price and our people that don't have the option of shifting will have some real problems.

What kind of assumptions did you make? In other words, if the total farm base goes into effect, what kind of assumptions do you make about how much maximum shift are we likely to see in any given year from other production acres, production of other crops over to say production of wheat in a year in which that appeared to be attractive, and what kind of assumption did you make about what that kind of shift would do to market prices?

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[14] This hearing was held on February 14, 1990, on the 1990 farm bill, chaired by Senator Boren at the Hoover Building, at the Garfield Company Fairgrounds, Enid, OK. The hearing was not printed.

I assume you ran some internal studies and made some studies and made some assumptions before making a proposal as sweeping as this.

Mr. **Gardner**. Well, of course, there have been many studies over the years of how farmers shift among crops in circumstances when they had more flexibility than they have had now. And one of the striking things that you see over many, many years is that it is quite unusual to see very large swings in acreage from year to year.

Just to consider your particular case of a producer of a commodity where there is no very good alternative, say it is wheat in your State, how could a problem arise for such a producer? If demand is strong, that would be the situation when you would see some expansion of acreage, people wanting to grow more wheat in response to the market. They may grow some wheat on some acres that weren't in the program before. You can't do that, you say, perhaps because of limitations, but our flexibility proposal does allow you to move on to the acreage ACR land.

Senator **Boren**. I understand that, but, of course, just basic supply and demand, the more supply you have, even if you have strong demand, means the less price increase you have in those years in which those farmers are trying to recoup. I notice at the end of your testimony you said that "our 1990 Farm Bill proposal most likely would result in more wheat production, greater exports, and some stock rebuilding, compared with an extension of the 1985 Act programs."

So I guess what I am asking is, did you do any internal studies at USDA to try to determine how much shift there would be, and how much do you expect, how would you quantify the additional wheat production that you make reference to here at the end of your statement?

Mr. **Gardner**. Well, again, the key to a flexibility proposal is that producers will be able to respond to market conditions as they unfold. But taking 1991 say, which would be the first year of our proposal if it were enacted, we think the most likely order of magnitude in the case of wheat, which would be one of the larger acreage responses, would be on the order of 3 million acres, perhaps, more than we would have otherwise.

This would come, perhaps, 1½ million acres out of land that would otherwise be in ACR, or annual acreage retirement programs, or otherwise mostly from feed grains scattered around the country. That would have a price effect of perhaps 15 to 20 cents a bushel. However, of course, your wheat producers are going to be protected by the target price provisions, so we don't see an income loss because of that. We see a possible income gain because the people who are making these choices will be making them when the market looks propitious for making those choices.

And with respect to your point about losing the chance, the 1991 scenario. I am departing from that now to address your other question about the possibility of really high prices if demand is strong. Again, with a target price of $4 we are going to have quite strong demand for this to happen, and in the scenarios we have run you don't get market prices that high really for most of the plausible scenarios you can come up with. They get fairly close to it sometimes.

Senator BOREN. So you are saying you don't think there will be much of a shift in price because you don't expect price to outrun the target price protection; is that what you are saying?

Mr. GARDNER. I expect that sometime in the next 4 or 5 years we will have an episode like we have had in the past where this will happen. It may be a drought, it may be a surge of demand from abroad, but when those things drive up prices, they are not things that the producers can plan for anyway. This would be something that would occur during the marketing year.

Senator BOREN. After the planting decision was made.

Mr. GARDNER. After the planting season, so you wouldn't see people planting in response to the high prices we will see. We may well see some high prices in the 1990's, I would be surprised if we didn't, but they won't be the kind of prices that are going to induce a huge acreage response, I would say.

Senator BOREN. Let me ask one other question, and then I will turn to my colleagues. I raised the point earlier about the Findley and the use of that 20 percent drop and, of course, when we have a market price say $3.20, and we drop the loan rate from $2.44 to $1.95, how do you explain why we have done this?

In other words, if the whole purpose of the Findley was strictly for competitiveness, why does that help us in terms of competitiveness if we are already below the market price considerably here, and doesn't it just upset the use by the farmer of the loan rate in terms of a financing mechanism?

Mr. GARDNER. Well, I think the idea of the marketing, or the Findley loan rate is not to put a level that is just below the market price. You need the potential there that if the market calls for it, we could sell at still lower prices than the current prices, move these commodities through the market while maintaining the income protection through the target price. And so I don't think we would want to set the loan rate just under the current market price.

Senator BOREN. Well, we were 80 cents below before we did the additional. That is a pretty significant difference already.

Mr. GARDNER. It is, but the wheat price can move 80 cents within the amount of time that elapses between when you set one of these loan rates and the time the following marketing year is done. You know, it is a volatile market and we want to be prepared for that possibility. I should say too that although the Findley provisions have caused the loan rate to come down, they won't cause it to come down any more. That is, if you go through with the formulas, there is not a real prospect that we would see the loan rate falling much more than that.

Senator BOREN. Well, does the Department believe that the nonrecourse loan still has a role in terms of providing interim financing? Is that something that is considered here?

Mr. GARDNER. Yes. I don't think we are writing off that as a method. But after all, if you take $1.95, that is a substantial fraction of the value of the asset that the farmer is borrowing against. In any kind of credit you are lucky if you get a full——

Senator BOREN. It is less substantial than $2.44 though if you are in an area where you are capital starved and you are trying to get the money in. I have a hard time believing we are going to have that big of shift that we are going to get below the loan rate, below $2.44.

Mr. GARDNER. Well, I would doubt if it will happen, and I hope it doesn't happen, but it is possible it may happen. And the idea of a market oriented loan rate is to be prepared if it does happen.

Senator BOREN. You still would have a lot of other tools to use, export enhancement and other authorities that weren't fully used last year by any means.

Mr. GARDNER. You do, but I think that the loan approach to this is, over the long term, a preferable approach.

Senator BOREN. Well, let me just sort of mark myself down as to where I stand on this and sort of raise a red flag that as one that has not fought the use of the Findley, and I understand the concept, I don't quarrel with what you are saying philosophically in order to keep us in the market, I just think that extreme caution should be used in how it is implemented, because if it is implemented in a way in which it is not been being very carefully tied to competitiveness criteria, particularly when we haven't used all of our export enhancement authority and the rest, I do think that it gives it a bad name to some degree because it reduces its capability in terms of the financing mechanism.

So I think in order for it to stay on the books, which I am not opposed to its staying on the books, I think the Department has to take real care to implement it properly. And I just have to say that in this case it does raise some questions in my mind as to whether or not it has been quite appropriately administered to have dropped it that much more.

Mr. GARDNER. Well, I would be glad to take a look and just see. I haven't seen a very detailed assessment of just what are the probabilities that one would get in trouble with a loan rate higher than that.

Senator BOREN. Senator Daschle.

Senator DASCHLE. Thank you, Mr. Chairman.

Mr. Gardner, the Findley questions posed by the chairman are ones that concern me as well, but they are indicative I think of other concerns that some of us have with regard to our policy in wheat. Another indication of the concern that I had, with regard to goals in particular, came about 6 months ago, less than that, when the Department announced that wheat farmers could modify their contracts, going from what they have under ARP all the way to 5 percent above their base in wheat in order to accomplish some newly stated goals that the administration had, expressed concern about carryovers, and maybe even price, I don't know.

But it goes to the point I was making in my opening remarks. I would be interested in your explanation as to what the administration's motivation was with regard to the 5 percent increase in wheat base? I mean, obviously it had a profound effect, and was that the effect intended? Did it backfire? Were you pleased with what happened? I would be interested in your response.

Mr. **Gardner**. Well, I thought your point in your opening remarks was a very good one, that it is good to think about the goals you have for your programs in agriculture, and in particular in this case the wheat program, what is it that we want to accomplish with this program? And I think in some ultimate sense what we want is a healthy agriculture, and we want a healthy wheat industry in this case.

Senator **Daschle**. How is that defined? That is the question.

Mr. **Gardner**. Well, I would define a healthy wheat industry as farmers earning a return from that activity that fully justifies their investment in the business and generates a reasonable standard of living comparable to other people in the sector, and these sorts of matters. The question though is how do we fit policy in with these ultimate goals?

And if you like, the proximate goals that we have in order to have the economically healthy sector we would like, it seems to me, involve competitiveness as one of the key factors. And it is that sort of search for competitiveness that I would say is the primary motivation behind the modified contracts, the notion there being that with fairly tight supplies of wheat compared to what we have had in the past, we want to be able to be sure that we have wheat to market and to be a factor in the world market, because that is where we are going to be getting our income from over the long term.

We don't want to encourage other countries to expand their acreage, as Senator Boschwitz pointed out many of them did in the 1980's, and so from that point of view we see competitiveness as extremely important, having supplies available being a key element of that. And I think that is really the motivation behind the modified contracts.

Now, as to whether the program has been a success, the Winter wheat plantings report, of course, showed 57 million acres, I believe it was, of Winter wheat seedings, which was somewhat less than had been anticipated, but more perhaps than we would have had otherwise, and we may have gotten a million acres or so out of that program so far. I wouldn't want to be too precise.

Senator **Daschle**. How close to your goal is that?

Mr. **Gardner**. Well, our goal was not a specific number of acres of wheat. Our goal was to provide some way of getting a little more assurance that we would have enough wheat to meet the market demands.

Senator **Daschle**. Well, it just seems to me that we could be a lot more precise than that. I mean, we have an ARP and we have a land diversion, we set loan rates, and we use those as our primary tools for influencing both stocks and price. That is really what our purpose is in utilizing those tools. And we are very precise with regard to the utilization of those tools. We penalize farmers for overextending ARP, or we argue, we haggle here about Findley and whether we are 80 cents or something else, and we even get emotional about loan rates. But then when it comes to the end result we are real general. We say, well, we are kind of—yes, you know, that is just in the ballpark.

And it just seems to me when we look at a new 5 year farm bill we ought to be able to do better than that. We ought to be able to say, you are right, this was a bull's-eye, this did exactly what we wanted. Even though no one could expect to be down to the last bushel here, but setting some policy goals with regard to stocks, what would we like?

I mean, it would be nice to have the administration or, frankly, anybody for that matter, come to the committee and say, this is what I think our target ought to be for carryover stocks for the coming year. This is what our target ought to be. We aren't saying we will get it, but we think these tools ought to be implemented to reach that kind of carryover target. We think these tools will do what we want it to do to reach other target for price.

But we don't get that, and just because we have never done it in the past, I guess I don't think that is a good enough reason not for us to sit down with the very best interest of agriculture at heart and really force ourselves to be a little more specific this year than we have been in the past.

Would you differ with that?

Mr. GARDNER. Well, I think that your general point is well taken, that both in what you do here and what we do in the administration of farm programs, we are forced into precision because we have to choose numerical values for target prices, we have to choose numerical values for ARP's, and in making those decisions we need numerical values on the market factors that are affected by ARP's and so on, like the carryover stock, like the level of production.

But nonetheless, I think that we are in a way forced into a false or impossible degree of specificity in doing that, because we have to come up with some way of calculating what we ought to do. But just inherently, because of weather, because of foreign demand, the things we cannot know, we know that things are not going to come out the way that our best estimate tells us they will.

And what do we do, seeing that situation? One thing you can do is to say, as you do, and I think it is a good point, that we should try to be as precise as we can, get the best information we can and do that kind of calculation and assessment better than we have ever done it before.

On the other hand, you can say that, look, we are never going to be able to predict these things precisely, let's don't pretend we can, let's leave it up to the market to make some of these decisions and provide a framework within which farmers and the markets generally can function and not worry about precise specification of things and then let the markets work.

Senator DASCHLE. Let me just respond, without monopolizing the time. That would be great if we had nothing to do with the market, but we do, and so we cannot argue, well, let's let the market decide, and then have a great debate about what the ARP is going to be, what the loan rate is going to be, whether we use Findley or not, whether we use a land diversion. And then say, well, we are going to decide all of that, and I am going to pound it out on this table, but then we will let the market decide what else happens.

What good does it do to argue all these tools if we don't also argue the goals? We all ought to have a decision here about what the goal is going to be, and then once we have decided the goals, I am going to be in a much better position to decide whether I agree with the chairman or the Senator from Minnesota on the ARP, or on the loan rate, or the paid land diversion. But we don't do that.

I guess I have said my piece. Thank you, Mr. Chairman.

Senator BOREN. Thank you, Senator Daschle.

Senator Bond has to leave to go to another committee meeting, so if it would be all right, I would like to turn to him for just a moment, because I know he has to leave.[15]

Senator BOSCHWITZ. I have to be somewhere at 3:15, too.

Senator BOREN. OK. Can I turn to him, and then we will turn right to you?

Senator BOND. Mr. Chairman, I apologize. We have contemporaneous hearings in a clean air matter I have to go to.

Again, Missouri ranked seventh in the Nation in wheat production. We are very much interested in this.

As I have mentioned in earlier hearings, we have had many meetings in the State where flexibility has been one of the most important things everybody has emphasized. We feel that flexibility is important for conservation compliance as well.

One of the things I wanted to bring to your attention, Mr. Chairman, and the attention of the subcommittee and the USDA, is more and more discussion of a normal crop acres concept with deficiency payments restricted to the commodity with the base. In other words, if you have a wheat base and you planted winter rapeseed, you could keep your wheat base but you would not receive the wheat deficiency payment. In other words, to allow flexibility without the possibility of program distortions.

At some time perhaps—my staff will be following these hearings—if you have a chance to address that, I would be interested to hear what the administration and my colleagues think of that, and also whether there would be a favorable impact on wheat by eliminating cross-compliance, which seems to be a major concern of our wheat producers.

Again my apologies to the subcommittee and my sincere thanks to you, Mr. Chairman.

Senator BOREN. Thank you very much, Senator Bond.

Dr. Gardner, any comment you would like to make?

Mr. GARDNER. Well, I would just say again, our principle for evaluating that kind of proposal would be does it involve the farmer in deciding on which crop to plant based on relative prices in the market or on target prices. And the difficulty I see with your proposal as you mentioned it was that by having to give up the deficiency payment on the program crop, then the farmer is going to have to be thinking about the market price for the rapeseed as opposed to the target price for the crop it is replacing.

Senator BOND. Which I thought was the goal.

Mr. GARDNER. But if you wanted to get the economically rational kind of substitution you would compare the market price for the rapeseed to the market price for the wheat.

Senator BOREN. Thank you very much.

Thank you, Senator Bond. Senator Boschwitz.

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[15] See pp. 203–204 for the prepared statement of Senator Bond.

Senator Boschwitz. I thank my colleague from North Dakota, and also you, Mr. Chairman.

I might say, Mr. Chairman, that flexibility as it is included in the bill that I have introduced includes, as you know, a flexibility not only in planting, but includes flexibility in both the loan and in the target price.

Senator Boren. Yes.

Senator Boschwitz. We have not only the loan at the Findley rate, but we have a recourse loan at 25 percent above the Findley, which would be the same as if the loan were reduced by 20 percent, so you go up 25 to get back to that same point.

In addition to that, we have flexibility in the target prices, as you and I have discussed. That is, that the estimated deficiency payment can be locked in in advance, so that a farmer would have a bankable situation. Now, of course, there is an estimate of the deficiency payment to come up with the prepayment of 40 percent. That entire estimated amount could be locked in in advance.

Flexibility goes beyond just the planting decision, it goes to the entirety of the program as we have introduced it. We call that recourse loan a harvest loan, that is the loan at 25 percent above the Findley.

I was wondering how many acres have been entered into the Secretary's program, or how many you anticipate will be entered into the Secretary's program of being able to increase to 105 percent?

Mr. Gardner. Now——

Senator Boschwitz. It is not quite clear yet.

Mr. Gardner. Yes, it is not quite clear yet, and we have made some changes that are intended to encourage a little more acreage, allowing people who undertake the modified contracts to sign up for 0/92 provisions. We think we will get even some more Winter wheat, and some more Spring wheat into this program. But what it will end up being, it won't be a big increase in acreage, but perhaps 2 to 3 million acres.

Senator Boschwitz. Two to 3 million acres.

Mr. Gardner. That may be overstating it.

Senator Boschwitz. What do you expect in the Dakotas, may I ask? Will there be producers who will increase, who will go for the Secretary's option?

Mr. Gardner. I believe there will.

Senator Boschwitz. It will be interesting, because one would think that they wouldn't. I listen often to my distinguished colleague from the other side, and one would think that that would not happen. So we will be interested to see how that develops.

I might say that in my thinking about flexibility, we thought about the impact on wheat, as you have pointed out, Mr. Chairman. We saw principally the impact that the programs had on soybeans, that soybean plantings went down about 10 percent, that the share of market that we used to have in 1970–71 was 80 percent of the world market, it went down, it is now down to 35 or 36 percent, something like that. And as we, through our current programs, prevent the interchange, which has some conservation advantages, of crops, others, Paraguay and Argentina and Brazil particularly, picked up more acres than we lost during that period. They picked up almost the entirety of the increase.

As I recall, in 1970 we were shipping 16 million tons of soybeans and in 1987 or 1988, I forget which was the last year, we were 20 million tons. To be sure, that is an increase of 4 million tons, but the world market had increased from 25 to 60 million tons, and I think maybe even more. Pardon me, it had increased, as I recall the figures, from 20 to 60 million tons, and our shipments had gone from about 16 to 20. So we went from 80 percent of the market to a third. And that is unfortunate, flexibility is intended to cover that.

We also thought, in thinking about wheat, that there was much marginal land, much dry land, if that's the right way to express it, that had been brought into production. This would balance out whatever shift there might be going to wheat because farmers would now be able to get the target price under the flexibility program that we offered, even if they didn't plant. They would be able to get the deficiency payment similar to 0/92, even if they didn't plant.

So my question is, in the event that deficiency payments were available to the producer, even if he didn't plant, would there be a reduction in wheat acres that would offset whatever movement there was toward wheat?

Mr. GARDNER. There would certainly be a movement in that direction. Whether it would completely offset, I don't know.

Senator BOSCHWITZ. In which direction?

Mr. GARDNER. A movement in the direction toward, as you say, having some farmers reduce wheat acreage because they would sign up for this program and take the deficiency payments and not plant wheat. But we do have the 0/92 program already, so there is——

Senator BOSCHWITZ. The 0/92 program, that can be use utilized in much the same way. In view of that, will there be this 3 million acre movement toward wheat? How much is in wheat now, 60 million acres, roughly?

Mr. GARDNER. More than that. We probably have perhaps 70 million planted.

Senator BOSCHWITZ. So that 3 million additional acres, when you are dealing with a commodity, is a substantial amount?

Mr. GARDNER. I think 3 million may be an overstatement, and I want to get a precise estimate. Three.

Senator BOSCHWITZ. Three.

Mr. GARDNER. OK.

Senator BOSCHWITZ. And any estimates on what will go out of production because of 0/92 or because the target price under a different plan might be paid in its entirety?

Mr. GARDNER. Well, I would say under 0/92 we may get 3 to 4 million acres in that program, but, of course, that was not a new thing that was introduced.

Senator BOSCHWITZ. I certainly agree with you, Mr. Chairman, that once we have moved toward a situation like we have, and that is that you have to use the base or you lose the base, and that you have to grow this crop, it is not without some complications to move away from it. I think it is necessary to move away from it, because I believe that decisions are made just as well out in Oklahoma as they are made here within the beltway, or in Minnesota; not particularly in North Dakota, I might say. [Laughter.]

Senator **Boren**. You will have equal time to reply to that, Senator Conrad.

Senator **Conrad**. I am eagerly awaiting that opportunity.

Senator **Boschwitz**. I am leaving.

Senator **Boren**. I already told you that our decisions were only as good as those within the beltway.

Senator **Boschwitz**. In any event, we thought that there would be not a movement toward wheat particularly, as we thought about all that, but we hoped that most of the movement would be among corn and soybean. That was what we were shooting for, because the soybean market is really one of the growth markets and I think it will continue to be a growth market. Of course, wheat is too, but not as quickly as soybeans, and so we wanted to be able to recapture some of that market.

Senator **Boren**. That 3 million acres that you talked about potentially shifting into wheat, did you say where you thought that would come from?

Mr. **Gardner**. I would say probably about half from the acreage that otherwise would have been idled in the annual acreage programs, the rest scattered around the country, but perhaps more feed grains than anything else.

Senator **Boren**. What percentage of acreage is that in terms of wheat acreage nationwide? What is that in total acreage?

Mr. **Gardner**. Four percent.

Senator **Boren**. So you are talking about a 4 percent shift or something like that?

Mr. **Gardner**. Yes.

Senator **Boren**. If you had a program that started us down this path with some sort of cap on it, I think Senator Pryor and others have talked about maybe a 10 percent cap with a shift or something like that, it probably would well accommodate what you estimate the shift would be, wouldn't it?

Mr. **Gardner**. It would accommodate it very well at the aggregate level. The problem is that when you make it apply to each individual farmer, that is the difficulty, because you will have some farmers who will want to do something quite a bit more than that. It is just that there will be many farmers who won't make any shifts at all. So in order to get even an aggregate 4 percent, you want to have some farmers have the ability, I believe, to do something quite dramatic with their cropping. Maybe they will try a new rotation, or something they never tried before.

Senator **Boren**. Is there a minimum percentage that you think you need to give on an individual farm basis in order to assure—in other words, is there some figure short of a wide open total farm base substitution?

Mr. **Gardner**. Well, I haven't thought about, and I don't think that anyone in the Department has really looked at the whole range of possible upper limits on this, but the way we did our "Green Book" was to allow complete flexibility. We did consider some 20 and 50 percent possibilities and thought that the 100 percent was the best.

Senator **Boren**. Yes, I understand. It is just a matter that there is a lot of apprehension, as you can imagine, in areas where you cannot have substitution.

Mr. **Gardner**. Well, I would like to get a better feel for that apprehension and really how widespread and deep it is, because——

Senator **Boschwitz**. You know, in the polls that I have seen, and what is the name—what happened to my staff back there?

Senator **Conrad**. They quit. [Laughter.]

Senator **Boren**. This is going to be a very interesting experiment, ladies and gentlemen.

Senator **Boschwitz**. According to a former member of the majority staff on the committee, some group that took a poll showed extraordinary approval of flexibility. It may not be totally understood. Its implications may not yet be, and that is part of our committee work.

Senator **Boren**. I think it is just like my own unscientific poll I took at our hearings we had in Enid with a couple hundred farmers there. There was a lot of support. Virtually everyone said, yes, we would like to see more flexibility. And then when you say, how many of you have some concern if we are able to shift the total farm base, then almost all the same hands went back up.

In other words, I think there is general support for flexibility. I am not sure that there isn't some level of concern as to a wide open 100 percent base possibility.

Senator **Boschwitz**. Was it in Enid you say? Do they have much flexibility?

Senator **Boren**. Most of them don't have much flexibility.

Senator **Boschwitz**. But yet they were for the——

Senator **Boren**. For some flexibility, but concerns about a shift of a whole base. So I don't know, there are some who I think would like to move us toward more flexibility, but some question about the overall.

Let me turn to Senator Conrad, because we are probably going to have a vote soon.

Senator **Boschwitz**. I am going to leave.

Senator **Conrad**. Before you leave, I just wanted to ask Dr. Gardner if he was familiar with the plan to idle the farm acreage in Minnesota as a means of preserving the lakes there for tourism? [Laughter.]

Senator **Boschwitz**. I knew I would get it.

Senator **Conrad**. Dr. Gardner, I want to take you back to a conversation we had earlier at a different subcommittee hearing, because the more I think about this and the more I talk to my constituents in North Dakota, the more disturbed I am at the relationship between inventories and price. Would you subscribe to the statement that prices are determined by the relationship between supply and demand?

Mr. **Gardner**. Yes, I would.

Senator **Conrad**. And that is the same answer that you gave at the previous hearing.

Mr. **Gardner**. Good.

Senator **Conrad**. Doing very well so far here.

Now, something is radically wrong then, because I just did a check on price. Last year we were getting $4.60 for Winter wheat. This year we are getting $3.86. Last year the ending stock was 700 million bushels. This year we are at 460 million bushels.

What is going on here? My farmers, every place they go they say we always hear price is supply and demand. Price is down, supply is down, who has repealed the law on supply and demand?

Mr. **Gardner**. I don't think the law has been repealed. The way I would explain it is that the supply side of the picture includes not only the ending carryover inventory that you are referring to, but you have to look at the production you had for that year. The total supply for the year includes the production plus what you carried into the year. And, of course, last year we were still working off the effects of the drought.

And the other side of the picture is on the demand side. What people are willing to pay and trade wheat for depends not only on current situations but expectations about what is going to happen in the next crop. And I think, as you have seen, a quite dramatic decline in the wheat price this year so far, 6 to 10 percent, depending on which price you look at, and it seems to me we have seen that happen as the prospects improve for the 1990 Winter wheat crop, as we have some moisture that we needed very badly in some areas.

So it seems to me that that is a hint that what is driving the process is the expectation of the 1990 crop more than the inventory level.

Senator **Conrad**. Well, I tell you, people out there have become highly suspicious of the way this system is working and have begun to wonder if there are not inventory management decisions being made by the administration to weaken price and decisions by those in the grain trade to weaken price. There is a very deep cynicism about what is going on.

When they see a dramatic reduction in ending stocks, a dramatic reduction in virtually any measure of carry over and supply-to-usage ratios, and yet the prices go down, it doesn't make sense to them. And then they see a proposal like that contained in the administration's budget that you are going to cut supports for wheat to $3.80 after a target price reduction from $4.38 down to $4.

What is it that the administration is going to do to send a signal to people out there that they care about farm income, or does the administration care about farm income?

Mr. **Gardner**. Yes, the administration cares about farm income.

Senator **Conrad**. You care about reducing it.

Mr. **Gardner**. No, no. We care about—in fact, I think in a way, our reason for being is to support agriculture and do what we can to encourage a healthy agriculture in this country.

Senator **Conrad**. Do you think agriculture is healthy in this country?

Mr. **Gardner**. I don't say that every farmer is healthy, or even every region, but for the overall picture I would say that agriculture is in reasonably good health overall, especially compared to where we were 5 years ago.

Senator **Conrad**. Well, I would invite you to my State. It is not healthy at all. We are facing slow economic strangulation, and I mean it is very serious what we confront. And there is a crisis atmosphere in my State.

I just finished a series of community forums on the question of farm policy. You could have cut the tension with a knife, because people look at where they are and where things are going, and I tell you, it is not just my State and others, we have tens of thousands of farmers in this country on the brink of bankruptcy.

I just don't see that as healthy, and frankly, I don't think there is an appreciation inside the beltway of what is going on out there. Your comments here confirm that; things are pretty healthy. I tell you, they are not healthy. We had better come up with something serious about turning things around out there or we are going to see an economic cataclysm out across the heartland of this country.

That may be apocalyptic terms, but you go out there and go town to town and there is a disaster, a slow motion disaster out there. This talk of cutting target prices from already low levels is just not going to do it.

Thank you, Mr. Chairman.

Senator Boren. Let me ask you, you mentioned $4 I think when you were talking about 1991. Is that the target price assumption on wheat?

Mr. Gardner. That is in the President's baseline.

Senator Boren. $4.

Mr. Gardner. Yes.

Senator Boren. If the target price stays the same—we are talking about freezing it in places I understand, the administration—we are seeing an escalation in costs, are we not, in terms of interest rates and other things? Wouldn't that tend to cause a decline of farm income if we were just simply to hold the same target price level?

Mr. Gardner. Well, I don't believe it would, because you would have to know how the costs fit in with yields and the whole picture of farm income. But let me say that the President's budget, of course, did involve a reduction in total spending in agricultural support. So that that question that Senator Conrad referred to about possibly reducing target prices, let me say that that is not the administration's position either. I am just pointing out that, as the Secretary has said, if you are going to meet the President's budget you are going to have to make some choices with some of the policy variables.

Senator Boren. Well, my concern is that if you then, say you go in at a $4 level, you freeze the target price level, if we have an escalation of costs, as we assume there is, and as we are beginning to see interest costs and other costs go back up, one of the reasons why the income levels were not worse under the 1985 act is in terms of what happened with costs during this particular period of time. There was less escalation of costs in some other periods, but it seems that in the last 12 months at least, in looking ahead, we may well see escalation of costs at a more rapid rate, which would then have a very negative effect on farm income than if we were still operating basically even under the 1985 act, than we would have otherwise.

Mr. Gardner. Well, I think if you look at the scenario that would lead to a rapid escalation in costs, it would be the kind of thing where energy prices might rise more, or some of the input prices rise more. The kind of scenario that would generate that would be a generally inflationary scenario, which I am not predicting, but if that occurred, usually in those circumstances you see the farm commodity prices rising also. So I am not so worried about being caught in an inflationary squeeze, at least in the short term.

But again, getting back to the target price question, I think that there is a fairly direct connection you can make between target prices and farm income in kind of a short term context, but when we are thinking about a farm bill that is going to stretch out over several years, I think we should avoid tying the prospective health of farming to target price levels, because, as we know, in the last 5 years we have seen budgetary costs come down and we have seen target prices come down while farm income is going up. And if we compare across commodities some commodities have had very substantial support price protection. Other commodities have had little or none, say in the livestock sector. And we haven't seen over the longer term that the producers of these commodities with very heavy support have become richer faster than the producers of the commodities that don't have such support. So I think we ought to think about when we have a longer term perspective, as we do at the beginning of a farm bill, it is good to address some of these things.

Senator CONRAD. Mr. Chairman, I really must say for the record that when we talk about farm income improving, we have just repealed the laws of inflation. In the decade of the 1980's we received the lowest net farm income of any decade since they started keeping records. All this happy talk in Washington that farm income is going up is just that. That is inside the beltway happy talk. The decade of the 1980's has been a disaster, and net farm income, if you account for inflation, has not been good. It has been the worst decade on record.

When you talk about the administration not advocating a reduction in target prices, well, we don't know what the administration is advocating because they won't say what they are advocating. The administration says cut the budget, but they don't tell anybody where. Now, we can play all these games and we can have very enjoyable conversations, but there is no there there. It is just talk. It is just conversation and doesn't mean a thing. And meanwhile people are in deep trouble.

Mr. GARDNER. Well, could I respond on the farm income question? I think what you want to think about—or at least one of the things—is what is the standard of living that we are generating for farm people, what kind of a standard of living can you earn as a farmer? And if you take the income of the average farm family, it has increased substantially in the 1980's in real terms. If you take your same numbers you were talking about and put them on a per farm basis, in 1989 we will have been at the highest farm income level, for income per farm family, at any time since maybe 1973 or 1974 were the only years that exceeded it. I mean, the real standard of living of farm people has improved.

Senator CONRAD. Was that a 1-year number?

Mr. GARDNER. Yes, that is 1989.

Senator CONRAD. Hey, let's talk reality. Let's talk the last 10 years. People have had a disaster in farm income, and all of this kind of talk about a 1-year number doesn't mean a thing. They built up debt in that 10 years, they saw their balance sheets collapse.

Senator **Boren**. I have to say, that is certainly the case. If you compare then how much additional debt they had to take on in the 1980's, and then you consider how much debt they are trying to service compared to where their income was for a 1-year period——

Mr. **Gardner**. But I don't think you want to compare our situation now with the mid-1980's. I perfectly well agree with you that the early 1980's were a very trying time in agriculture. I wouldn't want to see that happen again. We have very low incomes. We had all the problems you are talking about. But I do believe that those problems have been put behind us.

Senator **Conrad**. I can't let that go, Mr. Chairman, unchallenged. That just "ain't" the way it is. A recent North Dakota State University study shows we have dropped target prices so far that farmers will earn less than $13 an acre on wheat, and that is without compensation for labor and management—$13 an acre. If you have 1,000 acres of wheat, you earn $13,000 before any compensation for labor and management. I tell you, that is a disaster. And if this is progress, I tell you, you come out and visit my State and see what kind of progress we have had.

Senator **Boren**. We will have to stop the debate. It is a good debate, but we will have to stop at this point in order to go on. But I think that we have to consider also the fact that when we look at what the agricultural sector is being asked to do in terms of percentage of budget cuts, that is something that I don't quite understand. I don't see us cutting any other section of the budget the same percentage, even with changes in the world.

If you talk about an outcry, if you even suggested cutting the defense budget a fraction of the cost from the year before, compared to what is being talked about in cutting the agriculture budget, you are talking about an uprising. We would have a whole political revolution in the country in terms of what would happen if you had that kind of a proposal.

Let me say we do appreciate that you have been forthcoming with the estimates and numbers and some things that have been brought out here today that we haven't had access to before and we are appreciative of it.

Let me ask just a couple of very short questions. I understand, from my reading of the USDA farm bill recommendations, that the administration favors continuing the current rules on haying and grazing on the set-aside acres; is that correct, as far as you know?

Mr. **Gardner**. Yes, but we do have a multiyear set-aside proposal that will involve some different type of rules.

Senator **Boren**. But basically you will allow haying and grazing to continue; is that correct?

Mr. **Gardner**. On the annual acreage reduction program.

Senator **Boren**. On the CCC stocks, as I was mentioning awhile ago with the Export Enhancement Program, we are using the generic certificates in terms of the Export Enhancement Program. I think a number of us have been watching in terms of the level of stocks.

Is there a level of stocks which we might get, a low level of stocks on which it becomes very difficult, in your view, for us to continue to use the generic CCC certificates? And if that is true, is there any thought being given to alternative ways of making sure we can continue an effective Export Enhancement Program if we do get our carryover stocks at a certain low level beyond which it might not be practical to use the generic certificates? Is there some thought being given to that in the Department?

Mr. GARDNER. Well, of course, we are thinking about how to run export enhancement programs under a low stock regime.

Senator BOREN. Is there a possibility that you might consider some substitute for using the generic certificates, a cash substitute or some other kind of substitute?

Mr. GARDNER. Well, the problem is that the only real substitute is cash, and then you are in a different kind of program.

Senator BOREN. Right. Well, I assume that we wouldn't just automatically say, well, if stocks got down to a certain level we will discontinue EEP, we would look at the alternative of cash.

Mr. GARDNER. We would look at the alternatives.

Senator BOREN. Senator Kerrey, we are going to have to go in a minute. Are there any questions you would like to ask?

Senator KERREY. I believe it is important to point out that the proposals, the guidelines, run the risk, because they are largely budget driven, of seeing us repeat the mistakes that occurred in 1981 when USDA tried to keep the program at a very low cost and ended up with a very expensive program because surplus stocks were allowed to grow. I think your objectives have to go beyond the gross number of net farm income that doesn't convey either the historical progress in the 1980's nor does it represent the individual distribution of income among producers. I urge you as you look at the numbers to perhaps break the numbers out in a bit more detail.

I have a question that doesn't necessarily need to be answered now, Mr. Chairman, but I would like to get an answer to it. On the 13th of September, as you recall, Dr. Gardner, the USDA announced that wheat producers would be allowed to plant 105 percent of their base in exchange for reduced target price protection. Since that time we have had about a 20-cent decline in the per bushel price of wheat.

I am looking for the specific authority, the legal authority, under which the Secretary made that decision. I am trying to discover what specific provision in the current law gives the Secretary the authority, after the permanent program is announced, to take that kind of action.

Mr. GARDNER. I will be glad to convey that question.

Senator KERREY. I appreciate it.

Senator BOREN. Thank you very much, Dr. Gardner, and thank you for being forthcoming in your answers to our questions. We appreciate your being here.

[The prepared statement and attachments of Mr. Gardner follow:]

STATEMENT OF
BRUCE GARDNER
ASSISTANT SECRETARY FOR ECONOMICS
U.S. DEPARTMENT OF AGRICULTURE
BEFORE THE
SENATE AGRICULTURE SUBCOMMITTEE ON AGRICULTURAL PRODUCTION AND STABILIZATION OF PRICES
MARCH 8, 1990

Mr. Chairman and Members of the Subcommittee, I welcome the opportunity to discuss wheat and the 1990 Farm Bill. I will discuss the current U.S. and world markets for wheat and the Administration's proposal for the 1990 Farm Bill.

U.S. Wheat in the World Market

World wheat production has more than doubled during the past three decades, rising from 230 million metric tons in the early 1960's to around 535 million in 1989/90. Wheat production rose more than a third in both the 1960's and 1970's but has slowed in the 1980's, growing by a fifth. The slowdown in wheat production in the 1980's resulted from reductions in area harvested, particularly in the United States. As a result, the U.S. share of world wheat production is now slightly more than 10 percent, down from 15-17 percent in the early 1980's.

World wheat trade (excluding intra-EC trade) has grown from 45 million tons in the early 1960's to an estimated 98 million this season. From the early 1970's to the early 1980's, world trade nearly doubled. World trade exceeded 100 million tons for the first time in 1981/82 and peaked at 107 million tons in 1984/85. The U.S. increased its share of exports the most during the 1970's, because we were able to increase production more rapidly than our competitors. Since the late 1970's, the European Community (EC) has made the largest gains in world wheat trade, as their exports have more than doubled.

American farmers supplied about 45 percent of the wheat in world trade from the early 1970's to the early 1980's. This percentage declined in the mid-1980's to around 30 percent, but returned in 1987 and 1988 to around 40 percent with the aid of a lower wheat loan rate and Government export programs. However, total world trade in 1988/89 and 1989/90 is nearly 10 percent less than the record set in 1984/85, because Soviet imports are smaller. The U.S. share of world trade at 36 percent is also lower this season, reflecting tight U.S. supplies.

Domestic uses of wheat include food, feed, seed, and industrial uses. About 60 percent of domestic use of wheat is for food, by far the largest component. However, whenever wheat prices have been low relative to corn, sharp increases in the amount of wheat fed to livestock have occurred. Normally, 40-45 percent of U.S. wheat production goes into domestic uses.

The demand for wheat for food uses is relatively unaffected by changes in wheat prices and in domestic economic conditions.

Future use will be closely related to population changes and the trend toward convenience in food consumption, and growth is unlikely to match gains in per acre yields. Thus, future growth of the U.S. wheat sector depends on increasing exports.

Wheat Under the Food Security Act of 1985 (1985 Act)

Excess stocks during the 1960s were gradually being worked down by the early 1970s when export demand suddenly exploded. This led to a period of food security concerns that coincided with market expansion through most of the 1970s. After 1982, global export demand softened, and U.S. prices were not competitive, due to high loan rates and the strong dollar. This resulted in a loss of market share and large U.S. wheat stocks. As a result, farm legislation in 1985 had a clear need to address problems of competitiveness.

The 1985 Act sought to expand markets, both at home and abroad. The Export Enhancement Program (EEP) was established to meet competition from subsidized EC exports. Since the inception of the program, $2 billion in EEP bonuses have been paid in connection with wheat and flour exports, about 80 percent of the total for all commodities. The exchange of CCC inventory and producer loans for generic certificates helped make U.S. wheat available at competitive prices and reduced government stocks. Lower loan rates, competitive prices, and strong foreign demand also helped push U.S. wheat total use to a record high in 1987/88.

The policies instituted under the 1985 Act have reduced the U.S. role in providing a floor for the world wheat market. However, what was true in the past is still true today--whenever the United States cannot provide wheat for the world market other exporters will take our share. We are seeing this happen to some extent in the current season.

In order to hold down program costs, acreage reduction programs (ARPs) have been necessary each year under the provisions of the 1985 Act. The Conservation Reserve Program (CRP) has also reduced wheat production. Under the CRP, erodible land is retired from production for a ten-year period. More base acreage has now been enrolled in the CRP for wheat than for any other crop. Currently, about 10.3 million acres of wheat acreage bases are enrolled in the CRP, an amount equivalent to a 10-15 percent ARP. The CRP represents a constraint on U.S. wheat production capacity, unless changes in farm programs are made to allow wheat growers to expand acreage whenever market prices signal a need for more wheat.

U.S., foreign competitors', and total world stocks have also fallen in recent years. The world stocks-to-use ratio for 1989/90 is projected at the lowest since 1972/73. The U.S.

stocks-to-use ratio is the lowest since 1973/74. Canada suffered from the same drought that devastated U.S. spring wheat in 1988, reducing their stocks to minimal levels. High world wheat prices and a stronger U.S. dollar allowed the EC to export with much lower subsidies than in 1986-1988. As wheat prices have increased, some importers have drawn down stocks instead of importing as much.

As we look towards the 1990's, tight world wheat stocks will likely encourage an expansion in world production. In the United States, as the prospect for increasingly tight global supplies became more apparent last summer, the 1990 wheat program was changed.

The wheat program, requiring a 5-percent ARP, was changed to give wheat producers the option to modify their contracts in order to be able to plant up to 105 percent of their base, if they were willing to forego deficiency payments on an acre-for-acre basis. The modified program and more normal yields will help stocks recover slightly from the unusually low level expected at the end of this season. Winter wheat seedings for 1990/91 are up only 3 percent. However, the effect of the modified program is likely to be seen this year in a higher-than-normal percentage of last fall's seeded area being harvested for grain, as well as an increase in spring wheat seedings.

Wheat 1990 Farm Bill Proposal

Acreage Flexibility:

Increasing the competitiveness of U.S. wheat, a major theme of the 1985 legislation, is also a feature of our 1990 Farm Bill proposal. Much of the success of the 1985 Act in increasing wheat exports came from making the large carryover stocks from 1985/86 available at world market prices. As I just discussed, the 1990's are expected to be different, with export growth depending on our ability to produce wheat and readily market that production.

For all its successes, there is a persistent problem with the 1985 Act. Current programs have not resulted in sufficient acreage flexibility, for example, for wheat growers who already are planting most of their wheat acreage base. And, the acreage flexibility that we have allowed has too often placed the producer in the position of responding to target prices or program provisions rather than market conditions.

We believe our production flexibility proposal would allow wheat and other crop producers to respond to market opportunities that arise in future years. As outlined in the "Green Book", the wheat acreage base would be part of the farm's Normal Crop Acreage (NCA), along with the bases for feed grains, upland cotton, ELS cotton, rice, soybeans, sunflowers, and rapeseed, including canola.

Under our proposal, to qualify for program benefits for a target price crop, such as wheat, the producer must comply with any acreage reduction program announced for that crop. Acreage to be idled under the ARP is expressed as a percentage of the individual program crop base on the farm. In addition, to qualify for any program benefits, the sum of plantings of NCA crops plus acres idled under ARPs cannot exceed the farm's NCA.

Within the farm's NCA, the producer can plant any combination of NCA crops with no loss of deficiency payments or loss of base acres for future benefits. For a target price crop, deficiency payment acres in any year are equal to the base acres less the acres to be idled under the ARP for the crop, regardless of the mix of NCA crops planted.

Additional flexibility is achieved by permitting producers to plant and harvest the program crop or other approved crops not in the NCA on acres normally idled under the program crop's ARP. In this case, the producer would give up an acre of deficiency payment eligibility for each acre of reduced acreage that is planted and harvested.

Our proposed program is not one of "decoupled" payments, as some have claimed. Under our proposal, producers' planting decisions have an influence on the level of payments they receive. As I just described, payments must be given up to plant on idled acres. Both payments and base acreage for future payments must be given up if a producer plants non-program crops or even harvests conserving crops for hay on NCA crop base. And, deficiency payments are not guaranteed--they are still tied to market prices.

Our proposal is designed to deal with shortages as well as surpluses. If needed to provide adequate supplies, the Secretary may permit producers to plant up to 105 percent of the crop base; this action would relax the constraint on total plantings of NCA crops. If needed to reduce excessive supplies, any program crop may be excluded from the NCA and treated individually with a crop-specific ARP. Authority for paid diversion programs also exists.

The NCA proposal would allow farmers to more fully respond to market prices, leading to greater production of crops in short supply, such as wheat this season, and less production of crops in surplus supply. Farmers would be able to adjust cropping patterns and increase their income from the market. There would be greater use of crop rotations with benefits for the nation's soil and the environment.

Several groups and individuals have said they like the principle of being able to switch program crops on NCA acreage, but worry about massive shifts in crop acreage that would destabilize prices. To forestall such shifts, some have suggested 10 or 20 percent limits on changes in program crop acreage so that a producer who grew 100 acres of wheat one year could grow at most 120 acres the next and still receive program benefits.

It would be a mistake to restrict flexibility in this way. True, a 10 or 20 percent shift is the most we are likely to need on an aggregate basis for the country as a whole. But many individual producers may want to make more substantial adjustments--perhaps switching completely from wheat to oats one year, say, or establish a new crop rotation. Why place financial obstacles in the way of farmers who want to try out something new or see a good market opportunity?

The fear that farmers will all rush lemming-like to one crop has no factual basis and I think is a serious underestimation of farmers' intelligence. As soon as any sizable fraction of farmers make the first step toward crop imbalance, through planting intentions or unusual seed or machinery purchases, the cash and futures markets will reflect the changing balance. This will give all participants a chance to re-think their plans within days or a few weeks. We see this sort of continual planning and readjustment throughout the pre-planting season in all crops, including many nonprogram crops which do not have any acreage or price-support restrictions.

No doubt these decisions are difficult and farmers do make mistakes. If overproduction does develop, our proposal permits the Secretary to pull a commodity out of the NCA and set binding ARPs as mentioned earlier.

In general, the idea that the government knows better than market participants and should try to rein in farmers through limitations and regulations is dubious both in principle and in practice. In fact, it may well be that most of the destabilizing decisions of the 1980's were made by government, not by farmers. So let's not limit flexibility on the grounds that farmers will mess things up if allowed to follow their interests as they see them.

Another superficially attractive but ultimately unattractive proposal is so-called "base substitution", in which a producer could build base by up to 10 percent, for example, with acreage shifts. This looks like even more flexibility, but these shifts would respond to target prices, not market prices. This distinction--between acreage flexibility in response to market prices as opposed to target prices--is crucial to achieving a truly market-oriented program.

Stocks:

The 1985 Act set projected carryover stock levels at which ARPs for wheat and feedgrains are triggered. For wheat the trigger is 1 billion bushels. Using fixed stock levels to trigger ARPs does not take into account changes in domestic use and exports over time. We believe it is more appropriate to trigger ARPs on the basis of stocks-to-use ratios.

Under our proposal for the 1990 Farm Bill, if the ratio of ending stocks to total use for the preceding marketing year is estimated to be more than 40 percent for wheat, the ARP level would be 12.5-20 percent. If the ratio is 40 percent or less, the ARP would be 0-12.5 percent. Under our proposal the cost to wheat growers of participating in an ARP would be less than under the 1985 Act, because they can raise wheat and certain other crops on the acreage which they are required to remove from production.

Turning to the wheat price support and storage programs, we propose extending the wheat price support rate formula in the 1985 Act, but with authority to market CCC-owned wheat whenever the market price reaches 110 percent of the loan rate. We propose substantial changes in the Farmer-Owned Reserve (FOR) program. These changes are intended to retain the positive aspects of the FOR--price support when prices are low and price stability--and eliminate the negative aspects--USDA interference in grain markets, complex rules and regulations, and the market uncertainties that now occur as market prices or reserve quantities approach legislated triggers.

Our 1990 Farm Bill proposal for the FOR includes replacing 3-5 year contracts with 9-12 month contracts, which would begin during the second half of the marketing year. Storage would be paid in quarterly installments rather than making one annual payment. Grain would no longer have to be pledged as collateral for a regular loan as a condition for entry into the FOR, although participation in the annual wheat acreage reduction program would be required. Maximum levels of grain in the FOR would be 300 million bushels of wheat and 600 million bushels of feedgrain. Decisions to enter grain into the FOR or remove wheat from the FOR would be left to the producer--there would be no price triggers or quantity triggers for entry or release and no required FOR minimum quantities. However, at the discretion of the Secretary, storage payments could be discontinued when market prices exceed 140 percent of the price support rate.

We think our proposal for the FOR complements our production flexibility plan. Commodities that are produced in response to market signals should not be locked away in storage programs where they overhang the market, yet are sometimes unavailable when needed. Our proposal will increase the competitiveness of

U.S. wheat and other grains by providing greater responsiveness in both production and marketing.

Budget and Deficiency Payments:

We intend to work with the Congress to develop a wheat program that both serves producers' needs and is fiscally responsible. Changes in the wheat target price or payment acres may be needed. We support continuing the 5-year moving average to determine crop acreage bases, however we propose to lag the base calculation one year so that the immediately previous crop year is not used. The current procedure is inequitable to winter wheat growers who must plant before their new base acreages have been computed. Regarding program yields, we believe they should be set no higher than the 1990 program yields, which is the average of 1981-85 program yields.

Under current law, whenever price support rates for wheat or feed grains are reduced under the so-called "Findley" reduction, any additional deficiency payments that result from lower market prices are determined based on the average market price for the entire marketing year. We propose to determine the marketing year average price after the first five months of the marketing year rather than waiting until the end of the marketing year. To do this, actual prices for the first 5 months and the normal relationship between these first 5-month prices and prices over the remaining 7 months will be used. The chief reason for the change is to reduce the administrative burden of making two payment determinations for each crop that is now necessary.

Some have suggested tightened payment limits or even a "means test" to withhold payments from the largest farms. Target prices, payment acres, and limitations on payments to larger farms are all elements of the equation by which budgetary exposure can be kept within an overall budget figure.

Suppose that meeting the budgetary target required a 15-percent reduction in total outlays on price and income support programs, which is roughly what the President's Budget as compared to the baseline would require. Assume we wish to reduce wheat program outlays by 15 percent. Using the 1991 crop year as an example, this could conceivably be achieved by reducing the wheat target price from $4.00 to $3.80 per bushel. Another approach would be to reduce payment acreage 15 percent for wheat. A third possibility that has been mentioned is to introduce a means test that would deny deficiency payments to any participant whose income from all sources exceeds some predetermined amount. Or, we could keep target prices, payment acreage, and other program provisions the same, and introduce a budget-reduction assessment of 15 percent applied to all wheat payments. Not to place all the adjustment on one policy instrument, a combination of, for example, a 10-cent target price cut and a 7-percent assessment on payments could be used.

The most difficult and controversial of these tools is likely to be the "means-test" approach. Aside from the fact that it would alienate farmers, agreement on how to design and administer the test would be difficult, to say the least. And we know from experience that it is difficult to achieve actual savings as compared to projected savings in this way. We stand ready to work with the Congress on ways to make the difficult choices on program provisions for wheat and other commodities.

Export Programs:

Turning to export programs, we propose extending the authority to replenish the Food Security Wheat Reserve (FSWR). The FSWR, created in 1980, was authorized at a maximum level of 4 million metric tons of wheat owned by the Commodity Credit Corporation. The FSWR has been used during FY 1989 and FY 1990 in order to make available desirable quantities of wheat as food aid under P.L. 480.

We also propose to extend the provisions of the Export Enhancement Program, but without mandated funding levels or commodity programming requirements. The EEP is an integral part of the U.S. trade policy strategy for achieving a successful

Uruguay Round agreement. At the conclusion of the Uruguay Round, the EEP will be reassessed.

Conclusion

The U.S. wheat market is currently facing tight supplies. If this condition continues into 1991/92--the first year under the 1990 Farm Bill--our 1990 Farm Bill proposal most likely would result in more wheat production, greater exports, and some stock rebuilding, compared with an extension of 1985 ACR programs. Ultimately, the amount of wheat produced under our proposal would depend on how farmers view market returns from wheat in relation to those from other crops. This means that wheat would be produced for market demand. We believe that is the way it should be.

That concludes my statement. I will respond to any questions you may have.

All wheat: supply and disappearance 1/

Year beginning June 1	1986/87	1987/88	1988/89 Estimated	1989/90 Projected
			Million bushels	
Beginning stocks	1,905	1,821	1,261	702
Production	2,091	2,108	1,812	2,036
Imports	21	16	23	20
Supply, total	4,017	3,945	3,096	2,758
Domestic				
Food	712	721	735	750
Seed	84	85	103	100
Feed and residual	401	280	137	165
Domestic, total	1,192	1,086	975	1,015
Exports	999	1,598	1,419	1,300
Disappear., total	2,196	2,684	2,394	2,315
Ending stocks	1,821	1,261	702	443
Ave. market price ($/bu)	2.42	2.57	3.72	3.80-3.90

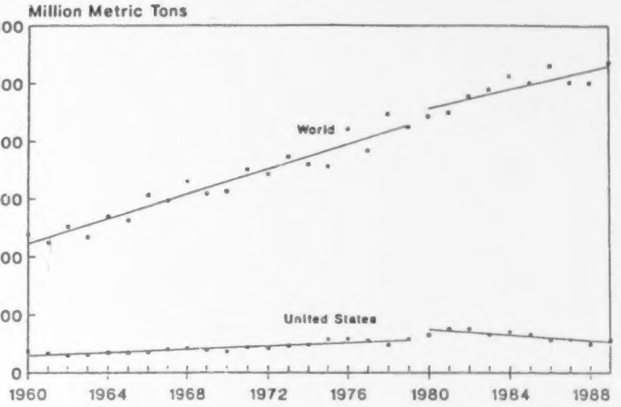
1/ Includes flour and products in wheat equivalent.

Wheat classes: Marketing year supply and disappearance, 1981/82-1989/90 1/

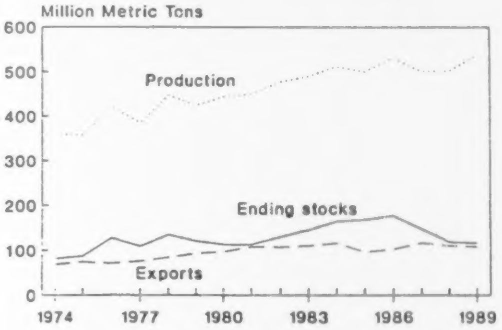
Year beginning June 1	Supply			Disappearance			Ending stocks May 31
	Beginning stocks	Production	Total 2/	Domestic use	Exports	Total	
	Million bushels						
1981/82:							
Hard winter	541	1,112	1,653	361	754	1,115	538
Hard spring	257	464	722	171	205	376	346
Soft red	38	678	716	196	460	656	60
White	93	348	441	62	270	332	109
Durum	60	183	245	57	82	139	106
All classes	989	2,785	3,777	847	1,771	2,618	1,159
1982/83:							
Hard winter	538	1,243	1,781	348	679	1,027	754
Hard spring	346	492	842	195	239	434	408
Soft red	60	590	650	251	325	576	74
White	109	294	403	53	207	260	143
Durum	106	146	256	61	59	120	136
All classes	1,159	2,765	3,932	908	1,509	2,417	1,515
1983/84:							
Hard winter	754	1,198	1,952	503	704	1,207	745
Hard spring	408	323	732	198	220	418	314
Soft red	74	504	578	284	220	504	74
White	143	322	465	78	220	298	167
Durum	136	73	212	51	62	113	99
All classes	1,515	2,420	3,939	1,114	1,426	2,540	1,399
1984/85:							
Hard winter	745	1,251	1,996	564	715	1,279	717
Hard spring	314	409	727	173	183	357	371
Soft red	74	531	605	289	252	541	64
White	167	301	469	86	210	296	173
Durum	99	103	206	45	61	105	100
All classes	1,399	2,595	4,002	1,157	1,421	2,578	1,425
1985/86:							
Hard winter	717	1,230	1,947	545	393	938	1,009
Hard spring	371	460	841	178	165	343	498
Soft red	64	367	431	204	148	352	79
White	173	254	428	80	150	230	198
Durum	100	113	216	42	53	95	121
All classes	1,425	2,424	3,864	1,049	909	1,959	1,905
1986/87:							
Hard winter	1,009	1,017	2,026	624	429	1,053	973
Hard spring	498	451	957	268	199	466	490
Soft red	79	292	371	180	114	294	77
White	198	232	437	77	175	252	185
Durum	121	98	225	49	82	132	95
All classes	1,905	2,091	4,017	1,198	999	2,196	1,821
1987/88 :							
Hard winter	973	1,019	1,992	514	911	1,425	567
Hard spring	490	431	925	268	255	523	402
Soft red	77	349	427	192	160	352	75
White	185	216	403	59	210	269	135
Durum	95	93	197	53	62	115	83
All classes	1,821	2,108	3,945	1,086	1,598	2,684	1,261
1988/89:							
Hard winter	567	882	1,449	507	639	1,146	302
Hard spring	402	181	590	176	195	371	219
Soft red	75	473	547	193	315	508	39
White	135	232	370	40	250	290	81
Durum	83	45	139	59	20	79	60
All classes	1,261	1,812	3,096	975	1,419	2,394	702
1989/90 3/:							
Hard winter	302	711	1,014	416	400	816	197
Hard spring	219	433	660	243	295	538	121
Soft red	39	548	587	224	340	564	23
White	81	251	336	73	210	283	53
Durum	60	92	162	59	55	114	48
All classes	702	2,036	2,758	1,015	1,300	2,315	443

1/ Data, except production, are approximations. Imports and exports include flour and products in wheat equivalent. 2/ Total supply includes imports. 3/ Projected.

Wheat Production: U.S. and World
1960-1989

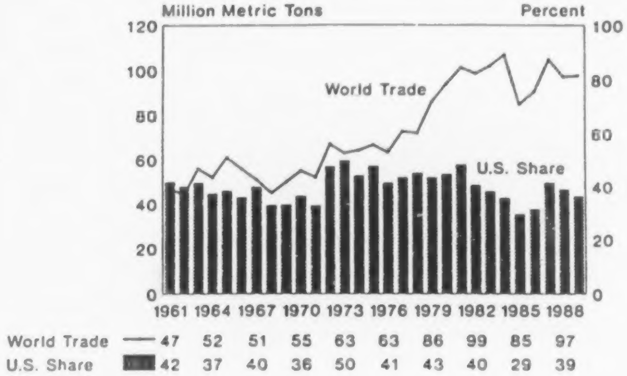


World Wheat: Production,
Exports and Ending Stocks

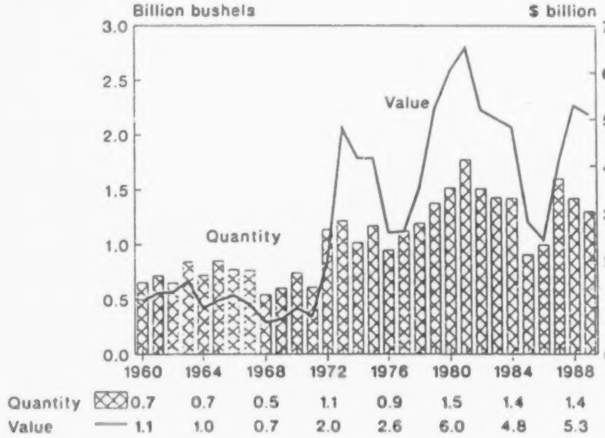


		1974	1977	1980	1983	1986	1989
Production	······	360	384	443	489	531	536
Exports	— -	68	76	97	110	102	108
Ending stocks	——	81	109	113	145	176	116

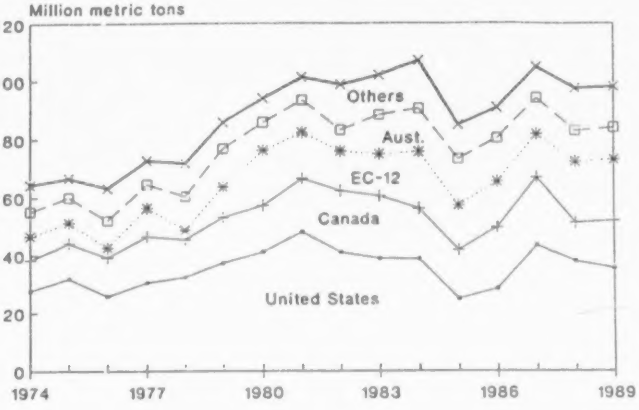
World Wheat Trade
Excluding Intra-EC Trade



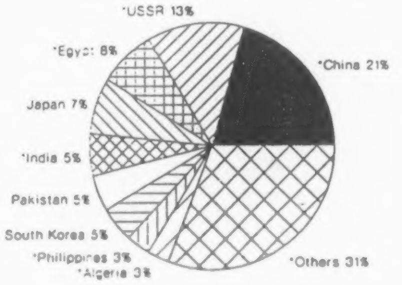
U.S. Exports: Quantity and Value



World Wheat Trade
1974-1989

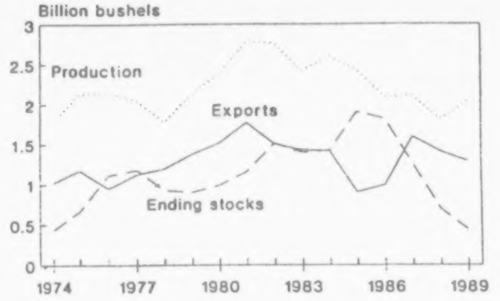


U.S. Wheat Exports by Destination
1988/89



* EEP recipient.

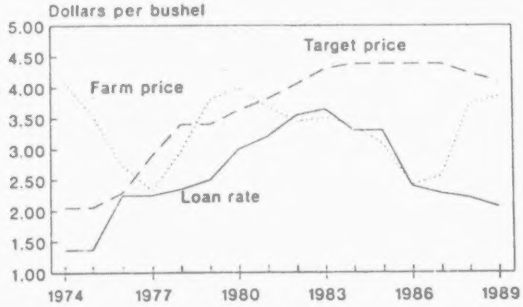
Wheat: Production, exports, and ending stocks, 1974-1989



	1974	1977	1980	1983	1986	1989
Production	1.782	2.046	2.381	2.42	2.091	2.036
Exports	1.018	1.124	1.514	1.426	0.998	1.3
Ending Stocks	0.435	1.178	0.989	1.399	1.821	0.443

Marketing year beginning June 1

Wheat: Farm prices, target prices, and loan rates 1974/75-1988/89



	1974	1977	1980	1983	1986	1989
Farm price	4.09	2.33	3.99	3.51	2.42	3.85
Loan rate	1.37	2.25	3.00	3.65	2.40	2.06
Target price	2.05	2.90	3.63	4.30	4.38	4.10

Marketing year beginning June 1

Wheat and Products: Net Budgetary Expenditures

Fiscal Year	Outlays	Receipts	Net Support and Related	PL480	Total
			($ million)		
1980	1,584.6	-706.0	878.6	666.0	1,544.6
1981	2,342.9	-800.3	1,542.6	719.3	2,261.9
1982	2,954.3	-716.8	2,237.5	630.8	2,868.3
1983	5,900.9	-2,482.0	3,418.9	704.7	4,123.6
1984	6,259.3	-3,723.2	2,536.1	628.4	3,164.5
1985	5,692.8	-1,002.0	4,690.8	851.9	5,542.7
1986	5,088.3	-1,648.6	3,439.7	714.7	4,154.4
1987	6,525.0	-3,688.6	2,836.4	607.0	3,443.4
1988	4,660.2	-3,982.3	677.9	550.2	1,228.1
1989	1,475.6	-1,422.5	53.1	696.4	749.5
1990a/	1,401.3	-878.9	522.4	509.0	1,031.4

a/ Estimate

Senator BOREN. We will be coming back. Why don't I ask Dr. William Tierney if he would come up to the table. We have a vote. We will be returning very quickly after that.

Dr. Tierney from the Department of Agricultural Economics at Kansas State University, we are very appreciative of your being here. I also know you have a plane to catch, and we will try to go expeditiously just as soon as we get back from the vote.

[Brief recess.]

Senator BOREN. We will go ahead and begin. I am sorry that we had this interruption. We had a vote and then the full committee off the floor for a moment. I hope some of our colleagues will be able to join us. But I assure you, Dr. Tierney, they will be aware of your testimony, whether they are here in person or not.

We welcome you. I introduced you as we were just breaking, and I would welcome you to go ahead with your statement at this time.

STATEMENT OF WILLIAM I. TIERNEY, JR., DEPARTMENT OF AGRICULTURAL ECONOMICS, KANSAS STATE UNIVERSITY, MANHATTAN, KS

INTRODUCTION

Dr. TIERNEY. Thank you very much, Mr. Chairman, I appreciate the opportunity to present testimony on the outlook for wheat and to answer any questions you may have. I do not have enough time—and I understand neither does anybody else—to address all the pertinent factors influencing the outlook of wheat, therefore, I intend to focus on the following issues: an apparent shift in the USDA's management of the U.S. wheat economy; the potential for U.S. wheat exports; stocks management policies; and production control measures.

In June 1986 the beginning stocks of U.S. wheat exceeded 1.9 billion bushels and prices averaged $2.25 a bushel. This year, wheat stocks will be less than 450 million bushels and prices should average $3.90 a bushel. The maintenance of this current favorable situation over the next 5 years will be difficult. I have prepared a more detailed analysis of the wheat situation, and that is attached to my statement.[16] Since you have that analysis, let me just highlight the conclusions here.

CURRENT SITUATION

With respect to the current situation, the recovery of the U.S. wheat economy was due to a combination of factors:

First, large U.S. set-aside requirements and the signup of 10.3 million acres of wheat base in the CRP; the U.S. droughts of 1988 and 1989; robust world demand and the influence of the Export Enhancement Program; and a temporary decline—and I emphasize temporary—in the wheat production of major export competitors.

I would like to address my comments now about the perception that, over the past several years, the USDA has been "managing" the U.S. wheat economy and has become—these are not my words, these are words that you see in many farm publications—"the

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[16] See pp. 265 to 287 for the testimony.

USDA has become a de facto Wheat Board." It may be useful to examine this perception more closely and to compare the USDA to another powerful government agency, that is, the Federal Reserve Board.

Both institutions, both the USDA and the Federal Reserve Board, exercise only those powers that Congress or the Constitution has mandated; both institutions seek to optimize the output of their respective economic sectors relative to a set of performance criterion which can often lead to contradictory results; and both institutions may have adopted a more aggressive management philosophy, their objective being to eliminate or dampen the cyclical tendencies of their respective sectors.

However, there are distinct differences between these two institutions, the USDA and the Federal Reserve Board. Besides the basic difference in their respective spheres of activity, the macroeconomy for the Federal Reserve, versus the wheat market for the USDA, there are two other noteworthy differences:

First, the USDA may have a more powerful set of policy tools than those available to the Federal Reserve; and second, the Federal Reserve enjoys a much greater degree of legislative immunity and independence of action than does the USDA.

EXPORT OUTLOOK

I would now like to talk a little bit about the export outlook.

The world's wheat trade has stagnated over the last 5 years and has been unstable due to the normal variability in world wheat production. Future U.S. wheat exports will be dependent on:

U.S.S.R. imports, which could remain constant or decline sharply if agricultural reforms in that country are successful; possibly smaller net wheat imports by the Eastern European countries—there has been a lot of enthusiasm about Eastern European import potential, I don't think with respect to wheat that there is good potential and I think possibly there could be a decline there; PRC imports, or the People's Republic of China, I believe could increase, particularly if per capita incomes in that country continue to improve; and finally, production by major competitors, who I do not expect will implement any *major* policy changes which would reduce their output—in other words, I do not expect that the GATT talks will result in significant changes there; and finally, the effectiveness of U.S. wheat subsidies in a market which I expect could return to a situation of excess production capacity.

I have a lot of graphs in the prepared testimony and you can look at those when you have the time.

STOCKS MANAGEMENT AND PRODUCTION CONTROLS

Let's get on to stocks management and production controls.

U.S. wheat stocks have been sharply reduced over the last 4 years. During this time, the USDA operated four different stocks programs simultaneously and managed these stocks using a variety of tools including: loan extensions, swaps, and PIK auctions. Stocks or inventory can play an important role in "managing" a market. Stocks can absorb supplies during periods of excess production and this, in turn, would support prices and reduce deficiency payments.

Or stocks can supplement market supplies when demand increases, and thereby moderate upward price pressures.

The Regular Loan and Farmer-Owned Reserve Programs may now be too restrictive and lack the flexibility to respond to changing market conditions. If the USDA intends to continue its "proactive" management policy, it will require a more flexible stocks release mechanism. With little or no stocks currently in the CCC inventory, the USDA does not now possess such a flexible stocks mechanism. In years when prices are low, there are pressures to permit stocks to grown in excess of whatever the "optimal" quantities are needed for market management. Unless safeguards are incorporated in any future stocks programs, there is no guarantee that stocks will not rebuild to burdensome levels.

Given my projections for world wheat market fundamentals, I see continued instability in world wheat prices. The United States will probably bear a disproportionate share of the burden of adjusting to this world market instability. This increases the probability that some kind of production restrictions will periodically be implemented.

"Fine tuning" the U.S. wheat economy as it adjusts to an unstable world wheat market may be difficult if the normal crop acreage proposal is accepted. Given the flexibility to plant a wide variety of crops without losing their deficiency payments, wheat producers may end up making their planting decisions based on *last year's* relative commodity prices. Wheat acreage could go up in years following high relative wheat prices and could go down in years following low relative prices. Unless we have a flexible stocks release mechanism that will compensate for these swings in production, wheat prices could be very volatile.

As I indicated, the rest of my testimony, including a bit more detail, is provided in the remaining materials.

Senator **Boren**. Explain further how you would modify what we are going now to have a more flexible stocks release policy? Spell that out for me.

Dr. **Tierney**. OK. First I have to indicate one thing. I come from a school of economic philosophy—and there are different schools—and this one is called the "positive" school versus the "normative." Normative economists are people that say, we should do this, or we should do that. Positive economists say, this is the result of this action or that action. So I am speaking as a positivist.

If one was looking for a flexible mechanism, one would want to be able to absorb stocks to whatever the predetermined optimal level is. Maybe that is 20 percent, 25, 30 percent, whatever your model tells you is the optimal level that would absorb year-to-year swings. Now, in a year you had overproduction, exceptional high yields, and wheat stocks wanted to go into that program, you would have to resist that pressure, because the evidence seems to be that, during the 1980's, there was no effort made to resist those pressures, and consequently we built up very huge stocks.

In those years you probably would have to allow wheat to go to another market. Wheat prices in very low price years tend to fall to the corn price, feed grain price. In those years you would see increasing quantities of wheat fed to livestock. Now, let's assume that the next year we had a crop problem here in the United

States, or in another major exporting country and demand increased. You would have to have a mechanism that would allow those stocks to come on to the market without a very dramatic rise in prices. Certainly not a $2 per bushel increase.

Because if you have the NCA proposal, a $2 increase in wheat prices is likely to increase wheat acreage that year, meaning that we go back again into an overproduction situation. In fact, economists, in introductory economics texts, they call this a "cobweb" market. You have swings in production and you are always dancing around the long-term market equilibrium and you never hit it.

So if you go to the NCA proposal—and it has its benefits—you would have to have, perhaps, a flexible compensating stocks mechanism which will absorb if there is overproduction and then release the next year. So that those swings that you get in production are offset by compensating movements or changes in stocks.

Senator BOREN. Given what you see as the volatility—well, let me ask this question. Given the fact that our stocks are at a very, very low level now, how long do you think it would be under a worst-case scenario in terms of international demand not escalating, international production going up, how long do you think it would be before we build back up to what you would view as very high levels of carryover?

Dr. TIERNEY. Well, I would like to direct your attention to a graph on page 2.[17] You can see that back in 1981–82 the black dot, which represents stocks, world wheat stocks were about 90 to 95 days supply, and 1981–82 was also the year that the United States achieved record exports of about 1.7 billion bushels, and we had about 48 percent of the world market. I also should emphasize that 10 years ago changes in the Kansas wheat crop condition was worth 20 or 30 cents in the wheat market. Ten years ago the United States was the world's second largest wheat producer. We are now the fourth largest. So today, we should not focus too much on just what is U.S. stocks, but more importantly, what are world stocks.

Now, you can see that it took 3 years to, 1984–85, when we had built stocks up to about 130 days supply, and it has taken us approximately 2 years since 1986–87 when we saw the major drop in stocks. You can also see the columns, on the graph, which indicate world trade, we did stall out at about 1981 and since then trade has had a pattern of being very volatile. In 1985–86 I think world wheat trade was only 85 million metric tons.

Senator BOREN. With this kind of possible volatility that we are looking at, then an Export Enhancement Program would be important in terms of maintaining our share of this market if we have this kind of volatility, would it not?

Dr. TIERNEY. That is true if the Export Enhancement Program is an effective program. I just was looking at an article that was published in the American Journal of Agricultural Economics which had tried to go back and simulate the transactions, the negotiations using some kind of gaming theory, and I believe 3 or 4 months ago the USDA published a study on the effectiveness of

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[17] See p. 253 for the graph, "World Wheat Stocks Have Collapsed to Their Lowest Level in 20 Years and Trade Has Stagnated."

EEP, and they estimated that there was an additionality effect, meaning that without the EEP program, wheat exports would have been 10 to 30 percent lower, depending on what year and what country.

I think it is extremely difficult to get any good analysis. In effect, what you have to be able to do, is like analyzing a poker game. You have to be able to look at everybody's hand, understand their psychology, see how much money is in their checking account in order to determine that the game could have been won by that individual, that individual, that individual.

So I probably agree with USDA that 10 to 30 percent is an acceptable additionality effect, but how they came up with that I don't know.

Senator BOREN. What about costs, as you look at cost of production over the next 5-year period? Have you done any studies or have access to studies that would indicate where we think the cost trends are going to go?

Dr. TIERNEY. I think it is more important not to talk about simply cost, but talk about farm income, which apparently Senator Conrad was extremely concerned about.

We have in the State of Kansas a farm management association of approximately 2,600 farmers. These are mostly large commercial size operations with average gross sales of about $170,000 a year. Four years ago their average farm income for the entire association was $5,000. That rose to about $20,000, then $40,000, and then last year $48,000. And this year it is probably going to be $50,000 give or take $5,000.

However, about 94 percent of the improvement in farm income in that 4-year time period was due to four categories. One category was lower interest expense due to a reduction in debt and lower interest costs; second was an improvement in livestock income, and certainly very important in Oklahoma; the third factor was lower depreciation, because when we do our farm accounts, we include total values, changes in inventories, everything. Well, a lot of farmers have been depreciating their machinery stocks down to very low levels. The fourth item was about a $15,000 increase in payments from the Government.

So 94 percent of the improvement in farm income was due to those four categories. What is going to happen to livestock income? Is it going to be profitable for the third year in a row? Depreciation is probably going to go up. Interest rates are going up, because they are going to have to borrow money. Some farmers are expanding operations as well. And what is going to happen to Government payments?

I think it is possible that the improvement that we have seen particularly over the last 2 to 3 years, may have peaked and the forces will probably be pushing farm income down again.

Senator BOREN. In interest and depreciation alone, and then if you assume a freezing of the Government payments relatively, so that there is not any additional increase, it would stand to reason that incomes probably have peaked, net income.

Dr. TIERNEY. That is true. Now, I was sitting here listening to Dr. Gardner, and I think this is terrible to have two agrieconomists in a row, one after the other. If the audience didn't fall asleep on the first one, they are bound to fall asleep on the second one. Anyway, Dr. Gardner had some very good points about an individual producer saying, "where can I maximize my income?" And as an economist looking at the micro economics of an individual producer, right now if I was a wheat producer in eastern Kansas, I would probably, if I had NCA available, be planting soybeans into my wheat acreage, because I can actually make a dollar a bushel profit on soybeans in eastern Kansas instead of losing money on wheat. I would make this switch if I was assured I would still get wheat deficiency payments.

However, I understand producers' concerns that we are going to just accentuate the swings in acreage from year to year. Again, a mechanism that I have not heard anyone mention is a bidding process, much like what happened in 1983 when farmers bid their entire farms into the, I think it was the PIK program, the set-aside, the 100 percent set-aside.

What if we set up a mechanism where a farmer who, let's say because of conservation needs or because of weed infestations or whatever, wanted to plant 100 percent of my wheat acreage to rapeseed or soybeans, and then he said, I will be willing to bid 15 percent of my deficiency payment, whatever it is. Then the USDA would still have the ability to allocate acreage to whatever farmer wanted it the most and set the total amount of acreage switching to a level that would not, in their estimation, cause undue variation in supplies.

So that way, Dr. Gardner's concern for the individual producer having access to maximum flexibility could be handled.

Senator BOREN. While we control the macro——

Dr. TIERNEY. And you allow the farmer to indicate how bad he wants it by bidding how much he is willing of his deficiency payment he is willing to give up.

Senator BOREN. Well, thank you very much. I appreciate the comments you have made and I will share them with my colleagues, and I apologize for keeping you so long that you are going to have to change your airline schedule now.

We appreciate your being here.

Dr. TIERNEY. That is all right. Thank you.

[The prepared statement, charts, and attached testimony of Dr. Tierney follow:]

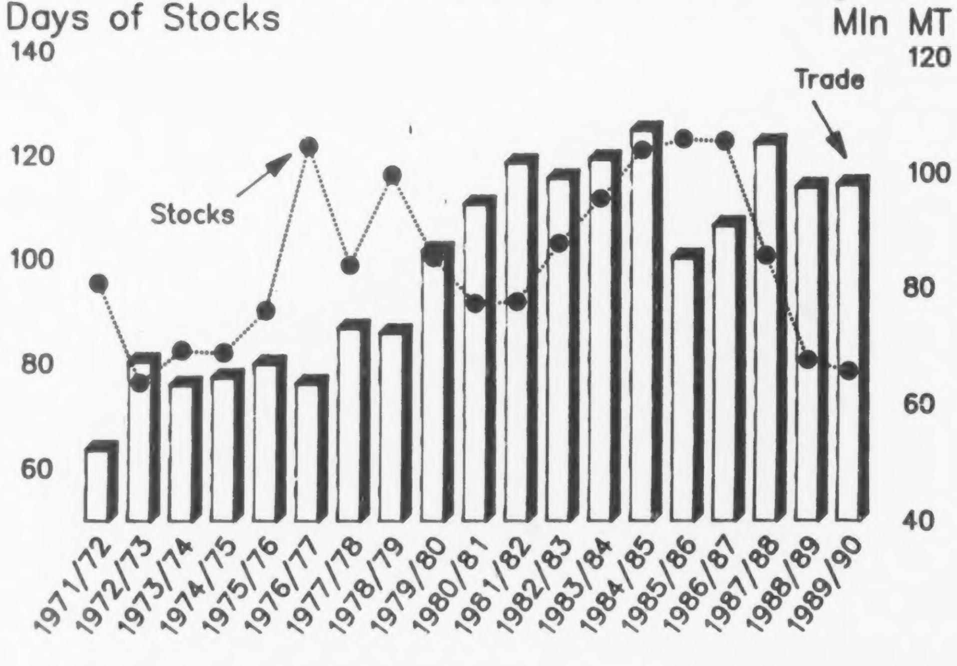
Statement by William I. Tierney, Jr.
Extension Agricultural Economist, Marketing and
Associate Professor, Department of Agricultural Economics,
Kansas State University
Before the Subcommittee on Agricultural Production and
Stabilization of Prices
Senate Committee on Agriculture, Nutrition, and Forestry
March 8, 1990

Mr. Chairman, members of the subcommittee, I appreciate the opportunity to present testimony on the outlook for wheat and to answer any questions you may have. I do not have enough time to address all the pertinent factors influencing the outlook for wheat, therefore, I intend to focus on the following issues:

- an apparent shift in the USDA's management of the U.S. wheat economy;
- the potential for U.S. wheat exports;
- stocks management policies; and
- production control measures.

In June 1986, the beginning stocks of U.S. wheat exceeded 1.9 billion bushels and prices averaged $2.25/bushel. This year, wheat stocks will be less than 450 million bushels and prices should average $3.90/bushel. The maintenance of this current favorable situation over the next five years will be difficult. I have prepared a more detailed analysis of the wheat situation and that is attached to my testimony. Since you

World Wheat Stocks Have Collapsed to Their Lowest Level in 20 Years and Trade Has Stagnated



have that analysis, let me highlight the conclusions here.

Current Situation

The recovery of the U.S. wheat economy was due to the combination of factors:

- large U.S. set-aside requirements and the signup of 10.3 million acres of wheat base in the CRP;
- the U.S. droughts;
- robust world demand and the Export Enhancement Program; and
- a temporary decline in the wheat production of major export competitors.

Has the USDA Adopted a More Active Management Role in the U.S. Wheat Economy?

There is a growing perception that, over the past several years, the USDA has been "managing" the U.S. wheat economy and has become a de facto Wheat Board. It may be useful to examine this perception more closely and to compare the USDA to another powerful government agency, the Federal Reserve Board.

Both institutions:

- -- exercise only those powers that Congress or the Constitution has mandated;
- -- seek to optimize the output of their respective economic sectors relative to a set of performance criterion which can often lead to contradictory results; and both institutions
- -- may have adopted a more aggressive management philosophy, their objective being to eliminate or dampen the cyclical tendencies of their respective sectors.

However, there are distinct differences between these two institutions. Besides the basic difference in their respective spheres of activity (the macroeconomy versus the wheat market), there are two other noteworthy differences:

- -- the USDA may have a more powerful set of policy tools than those available to the Federal Reserve; and
- -- the Federal Reserve enjoys a much

greater degree of legislative immunity and independence than does the USDA.

Export Outlook

The world's wheat trade has stagnated over the last five years and has been unstable due to the normal variability in world wheat production. Future U.S. wheat exports will be dependent on:

-- USSR imports which could remain constant or decline sharply if agricultural reforms are successful;

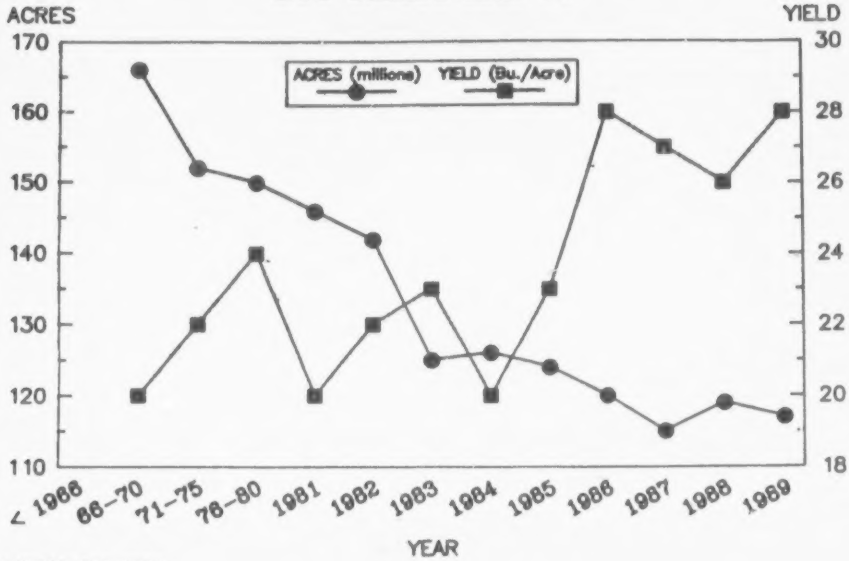
-- possibly smaller net wheat imports by E. European countries;

-- PRC imports which could increase particularly if per capita incomes continue to improve;

-- production by major competitors who are not expected to implement any major policy changes which would reduce their output; and

-- the effectiveness of U.S. wheat subsidies in a market which may return to a situation of excess production capacity.

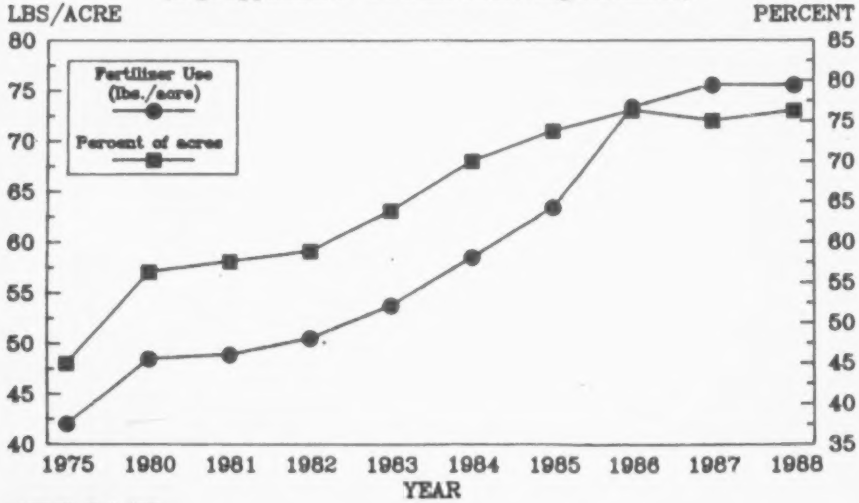
SOVIET WHEAT ACREAGE HAS DECLINED BUT YIELDS ARE UP



SOURCE: FAS, USDA

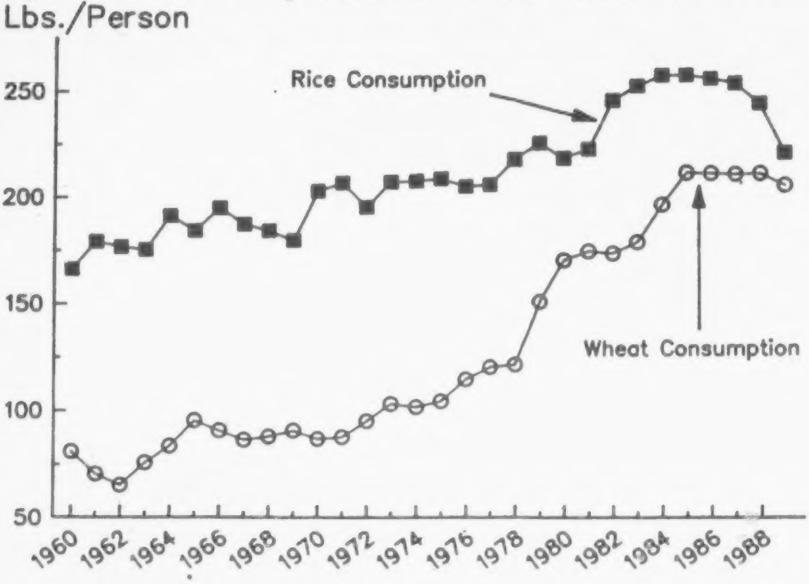
SOVIET USE OF FERTILIZER IS UP ON ACREAGE OF SMALL GRAINS AND PULSES

(Avg. application on land recieving fertilizer)

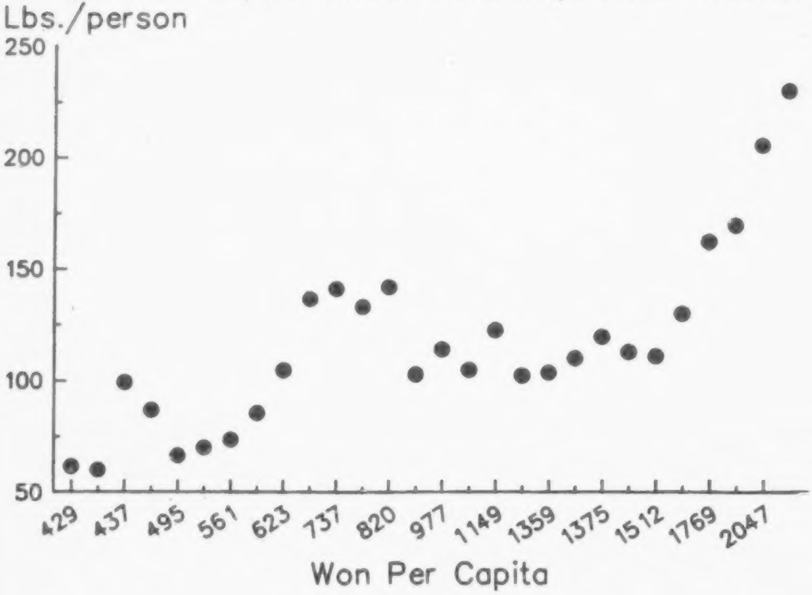


SOURCE: FAS, USDA
* Excludes corn which is less than 5% of all grain acres

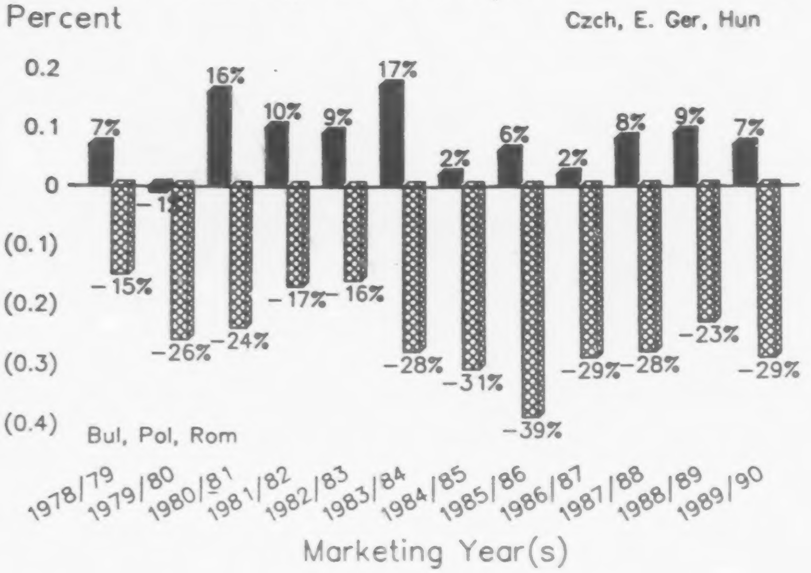
By 2000 China May Consume More Wheat Than Rice



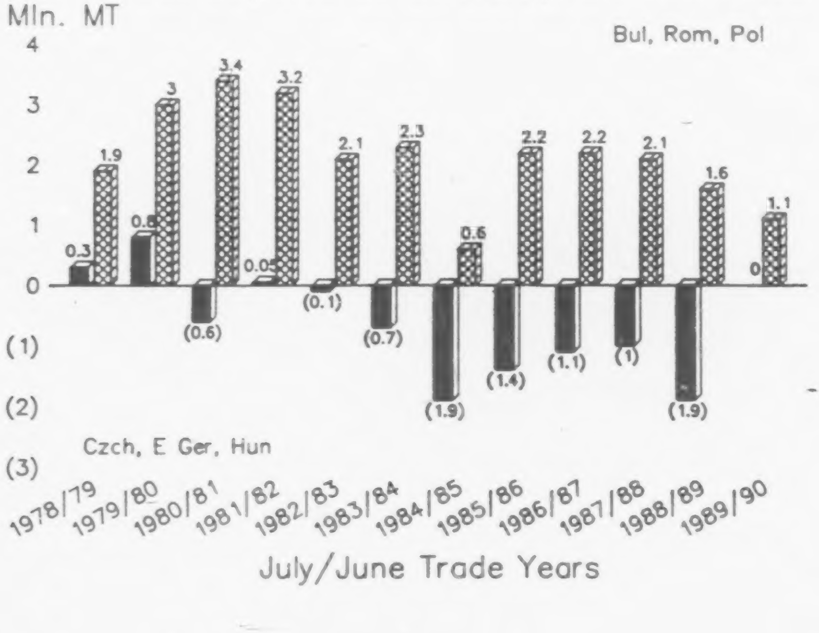
Korean Per Capita Wheat Consumption & Income



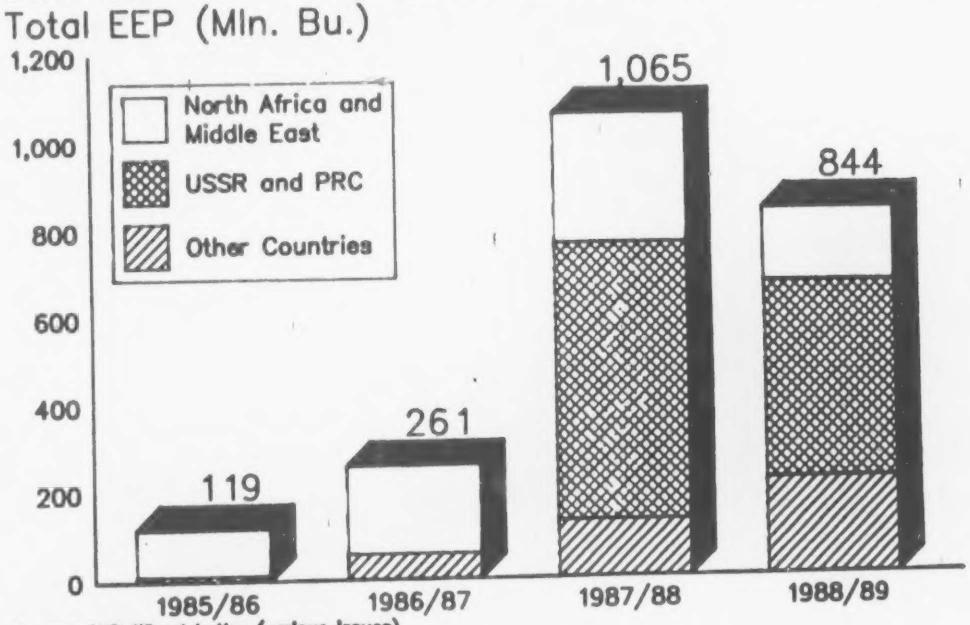
Wheat Yields, E. Europe Vs. EC-12



Net Wheat Imports of E. European Countries

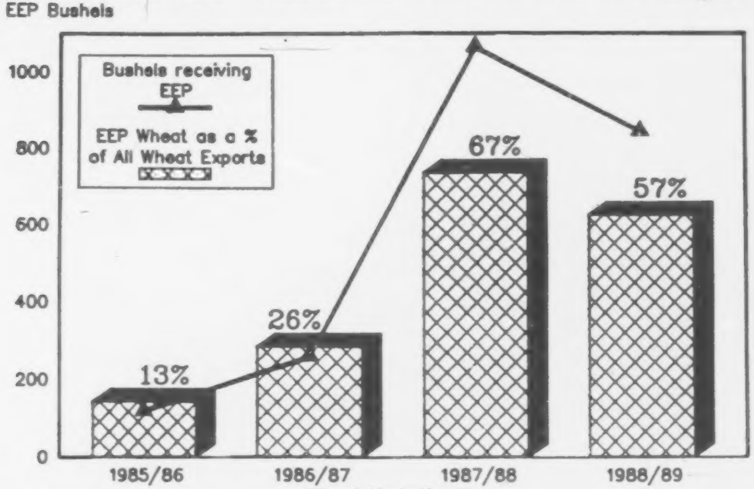


FOCUS OF EEP WHEAT
HAS SHIFTED SINCE THE INCEPTION OF THE PROGRAM



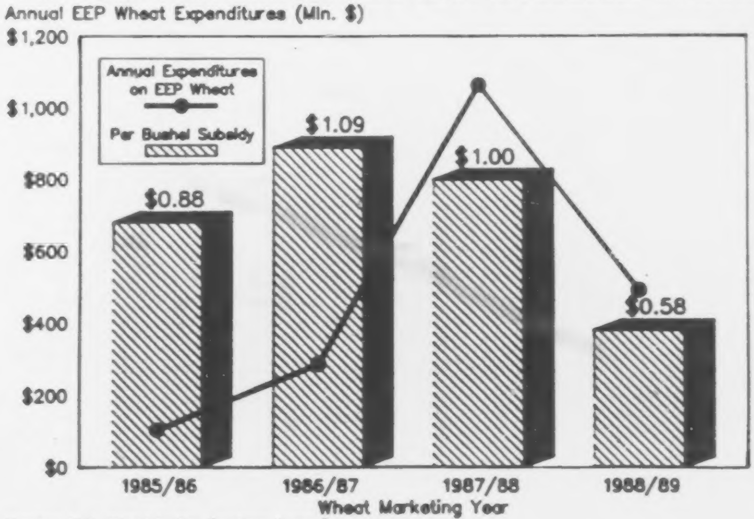
Source: U.S. Wheat Letter (various issues),
U.S. Wheat Associates

EEP WHEAT ACTIVITY -- Total Bushels Receiving EEP and EEP Wheat as Percent of All Exports



Source: U.S. Wheat Letter (various issues), U.S. Wheat Associates.

EEP WHEAT ACTIVITY
ANNUAL EXPENDITURES AND AVERAGE SUBSIDY

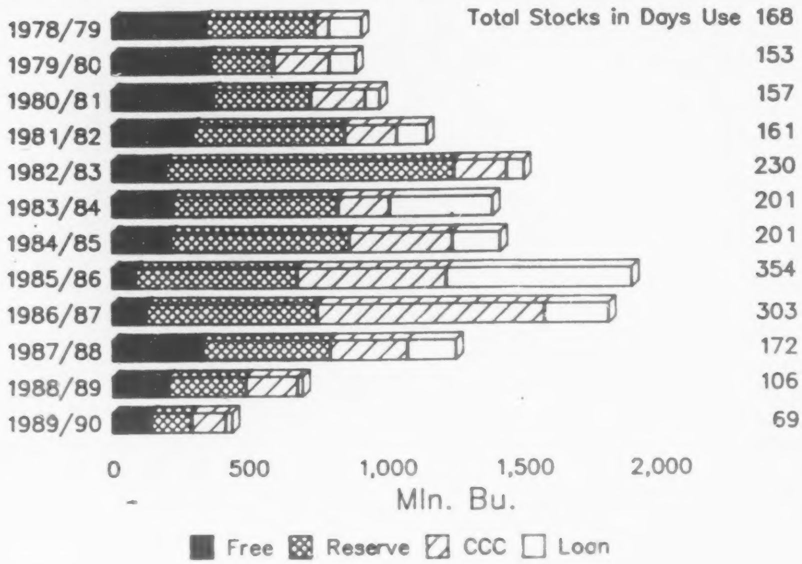


Source: U.S. Wheat Letter (various issues), U.S. Wheat Associates

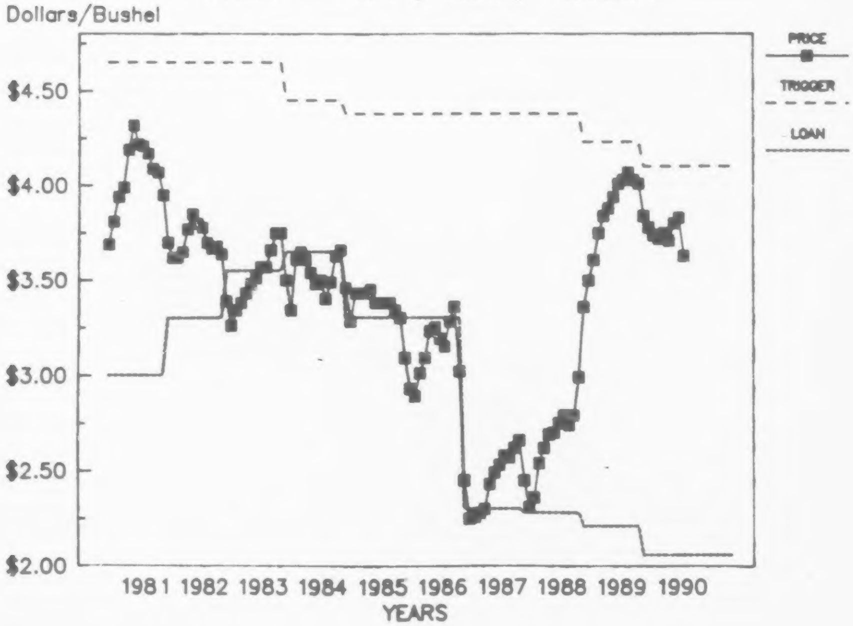
Stocks Management and Production Controls

U.S. wheat stocks have been sharply reduced over the last four years. During this time, the USDA operated four different stocks programs simultaneously and managed these stocks using a variety of tools including: loan extensions, swaps, and PIK auctions. Stocks (inventory) can play an important role in "managing" a market. Stocks can absorb supplies during periods of excess production and this, in turn, would support prices and reduce deficiency payments. Or stocks can supplement market supplies when demand increases and thereby moderate upward price pressures.

The Regular Loan and Farmer-Owned Reserve Programs may be too restrictive and lack the flexibility to respond to changing market conditions. If the USDA intends to continue it's "pro-active" management policy, it will require a more flexible stocks release mechanism. With little of no stocks currently in the CCC inventory, the USDA does not now possess such a flexible stocks mechanism. In years when prices are low, there are pressures to permit stocks to grow in excess of the "optimal" quantities needed for market management. Unless safeguards are incorporated in future stocks programs, Composition of U.S. Wheat Ending Stocks



WHEAT: PRICE, LOAN, TRIGGER



there is no guarantee that stocks will not rebuild to burdensome levels.

Given my projections for world wheat market fundamentals, I see continued instability in world wheat prices. The U.S. will probably bear a disproportionate share of the burden of adjusting to this market instability. This increases the profitability that some kind of production restrictions will periodically be implemented.

"Fine tuning" the U.S. wheat economy as it adjusts to an unstable world wheat market may be more difficult if the NCA proposal is accepted. Given the flexibility to plant a wide variety of crops without loosing their deficiency payments, wheat producers may end up making their planting decisions based on last year's relative commodity prices. Wheat acreage could go up in years following high relative wheat prices and could go down in years following low relative prices. Unless we have a flexible stocks release mechanism that will compensate for these swings in production, wheat prices could be very volatile.

Testimony by William I. Tierney, Jr.

Extension Agricultural Economist, Marketing and
Associate Professor, Department of
Agricultural Economics,
Kansas State University
Before the Subcommittee on Agricultural
Production and Stabilization of Prices
Senate Committee on Agriculture,
Nutrition, and Forestry
March 8, 1990

Current Situation

At the end of the this marketing year (1989/90), the U.S. wheat situation will have improved dramatically from what it had been just four years before. In June 1986, beginning stocks of wheat exceeded 1.9 billion bushels (an amount equal to nearly one year's total disappearance). Wheat prices that year averaged $2.25/bushel, the lowest they had been since 1977. By the end of this marketing year, wheat stocks will have declined to less than 450 million bushels. Commensurate with this reduction in stocks, wheat prices have climbed to nearly $3.90/bushel, the highest they have been since 1981.

This turn around in wheat fundamentals is due to several factors:

- four years of relatively large U.S. set-asides (averaging 22 percent of base) augmented by the enrollment of 10.3 million acres of wheat base in the CRP program;
- the U.S. droughts of 1988 and 1989;
- the expenditure of over 2 billion dollars on wheat export subsidies; and finally

- a 700 million bushel decline, over the last two years, in the wheat production of our major competitors ('87/'88 and '88/'89 relative to '86/87).

Whether the current favorable balance in wheat fundamentals can be maintained depends on a number of factors. I do not have enough time to address all these factors so I intend to direct my comments to the following questions: "Has the USDA adopted a more active role in managing the U.S. wheat economy?", "What is the potential for the U.S. wheat exports?", "Do we need a more flexible stocks management policy?" and "Will we need to continue production controls?"

Has the USDA Adopted A More Active Role in Managing the U.S. Wheat Economy?

Over the last four years, the USDA seems to have adopted an "interventionist" role in the wheat economy. The USDA has begun to actively manage (some say micro-manage) the U.S. wheat economy. Some industry analysts believe that this country now has a de facto Wheat Board. It may be beneficial to pause for a moment and make a comparison between the USDA and another powerful government agency, the Federal Reserve Board.

Both the Federal Reserve and the USDA exercise only those powers that they have been legislatively mandated. Both institutions possess a broad set of instruments which they use to influence and/or regulate activity within their respective economic sectors. Both institutions seek to optimize the performance of their sectors. The performance criterion that the Federal Reserve is concerned with include things such as:

- stable economic growth;
- low inflation;
- full employment; and
- an efficient and competitive economy.

The USDA's performance criterion include such things as:

- ensuring a safe, abundant, high quality, and stable food supply at a reasonable cost;
- equitable returns to agriculture;
- protection of our natural resources;
- preservation or enhancement of our rural social and economic structures; and
- an efficient and competitive agricultural economy.

When comparing the Federal Reserve and the USDA, which institution has the more powerful set of tools at its disposal? Consider that in the last five years:

- eighty-five percent of U.S. wheat producers have participated in voluntary acreage reduction programs, and in return received billions of dollars in deficiency and disaster payments;
- the CRP has reduced the nation's wheat base by 11 percent;
- the USDA has "auctioned" off hundreds of millions of bushels of wheat held in CCC inventory;
- from two-thirds to three-quarters of all U.S. wheat exports receive some kind of subsidy; and
- the USDA is currently engaged in international negotiations which, if successful, would lead to a fundamental restructuring of the U.S. wheat economy.

While the powers of the Federal Reserve are great, its relative influence on the nation's macroeconomy can not match the USDA's influence on the U.S.'s wheat economy.

Over the last 20 years, a cycle of shortage and surplus has plagued the U.S. wheat economy. Using the Federal Reserve analogy once again, we can compare the cyclical nature of the wheat economy to the pattern of recession and recovery in the nation's macroeconomy. Just as the Federal Reserve attempts to fine-tune the macroeconomy, so too, it seems, does the USDA try to fine-tune the wheat economy.

The major difference between these two institutions is that, to a large extent, the Federal Reserve has legislative immunity and an independence of action not granted to the USDA. Consequently, should the USDA miscalculate or be unlucky, it is possible that Congress could eliminate or alter substantially the USDA's policy instruments.

Export Outlook

U.S. wheat exports are determined by several factors:

- policies and weather in major wheat importing and exporting countries;
- the "competitiveness" of U.S. wheat exports; and
- the general level of world wheat prices.

The world price of wheat is determined by the interplay of total world wheat import demand and total world wheat export supply. World wheat prices are highly volatile, in part, because the quantity of wheat traded in the world market is very small relative to the world's overall wheat production. World wheat trade this year will be about 98 million metric tons. This quantity represents about 18 percent of the world's production of wheat. It is possible that the world's wheat production could vary by 3 percent or about 16 million metric tons a year. If this 3 percent change in world wheat production results in a 16 million metric ton change in world wheat trade, prices could vary wildly. World wheat trade increased by nearly 100 percent from the early 1970's to the early 1980's. However, for the last five years, world wheat trade has ceased to grow and has been very volatile.

The USSR and PRC. The prospect for further growth in the world's wheat trade is heavily dependent on the import demand of the Soviet Union (USSR) and the People's Republic of China (PRC). Together, these two countries account for over a quarter of this year's world wheat imports as well as a third of the world's wheat production.

If the Soviets can successfully implement their program of agricultural reforms, it is conceivable that they could become self-sufficient in the production of milling quality wheat. Although the USSR currently produces about a third more wheat than it consumes for food purposes, less than a quarter of the Soviet wheat crop is used for food. This is due, in part, to poor grain quality, transportation difficulties, and inadequate price incentives. If the Soviets' reform program is not successful, then their wheat imports from all sources should remain about the same with year-to-year variations due largely to the weather.

While future Soviet wheat imports are likely to remain constant or to decline, there does appear to be significant potential for steady growth in wheat sales to the PRC. Despite a 75 percent increase in wheat production since 1980, wheat imports by China have grown and could increase further if;

- economic growth in the PRC continues, leading to an improvement in per capita incomes;
- PRC policies to increase domestic wheat deliveries fail;
- PRC policies which permit increased reliance on imports to feed urban

populations are left intact; and

- the U.S. maintains and expands trade relations with the PRC.

Per capita wheat consumption has grown dramatically in China. Most of this increase is due to the jump in domestic wheat production but there is evidence that wheat consumption has displaced the consumption of other food grains. Also, per capita wheat consumption has grown relative to rice consumption. There is no good source of income statistics for China, but an analysis of Korean data indicates that Asian wheat consumption rises sharply as incomes increase.

Eastern Europe. The recent events in Eastern Europe have raised questions regarding the future prospects for increased grain exports to that region. The agricultural economies of six of these countries can be expected to undergo profound changes. These countries are Bulgaria, Czechoslovakia, E. Germany, Hungary, Poland and Romania. Little or no change is expected in Yugoslavia or Albania. A by-country analysis of these countries reveals that all six have the potential to become significant importers of soybeans and/or soymeal. These countries may also increase their imports of feedgrains. However, it is likely that the region will become self-sufficient in the production of wheat. Three countries (Czechoslovakia, E. Germany, and Hungary) have relatively good wheat yields which, on average, are 7-10 percent higher than EC-12 wheat yields. In addition, these countries have been net exporters of between 55-70 million bushels per annum during the last few years. In contrast, Bulgaria, Poland and Romania have relatively poor wheat yields which have averaged 25-30 percent below the yields of the EC-12. These countries have been net importers of between 55-80 million bushels per year.

To varying degrees, agricultural efficiency in these countries may be 20-50 percent below it's potential. However, it may be inappropriate to presume that E. European agriculture can and should be able to achieve yields comparable to those of the EC-12. Economic restructuring of the E. European economy could eliminate many of the existing price distortions and subsidies.

If E. European agricultural inputs and commodity prices are allowed to fluctuate along with world prices then we may see a disinvestment in E. European agriculture. The EC-12 has a very wealthy and productive economy which can easily afford the massive cost of their Common Agricultural Policy. It may be impossible and certainly undesirable for the E. European countries to spend their scarce resources to subsidize agriculture to anywhere near the extent it is subsidized by the EC-12.

Future E. European demand for wheat is unclear. Per capita flour consumption in these countries is two to three times higher than in the U.S. and if real incomes increase, flour consumption may fall while the demand for meat, fresh fruits and vegetables may rise. However, regardless of potential changes in the wheat supply and demand of these countries, it is likely that like Western Europe, they may increase their imports of high protein and durum wheats.

Export Competitors. As previously noted, the combined wheat production of our major export competitors declined by nearly 700 million bushels over the last two years, (1987/88 and 1988/89). This year (1989/90), our competitors combined production is up by 550 million bushels from what it was a year ago. Over the last six years, the U.S. has reduced its production while our competitors did little to reduce theirs. This year, the EEC harvested a record acreage of wheat. This increase in acreage follows the record exports that the EEC was able to achieve last year (950 million bushels). It seems likely that the wheat production of our major competitors will remain at current levels or expand. Of course, year-to-year variations in weather could effect their output, but I do not anticipate that they will implement any major policy changes that would lead to a significant cut in their combined production capacity.

The Competitiveness of U.S. Exports. In the early 1980's, approximately 15 percent of all U.S. wheat export sales were made with the assistance of export programs such as PL 480 and Export Credit. However, with the introduction of the Export Enhancement Program (EEP) in 1985, some form of export assistance has been provided for ever increasing quantities of U.S. wheat exports. At first, the EEP program was used sparingly and targeted primarily to North African countries where competition from EEC subsidized wheat was most intense. Beginning in 1986/87, the program was expanded to include nearly all our traditional customers with the exception of most of Western Europe, Korea, and Japan. By FY 1987/88, nearly three-quarters of all U.S. wheat exports received government assistance and nearly one-third received subsidies from more than one program (ie EEP and credit guarantees). Total EEP expenditures for wheat rose to just over $1 billion during the 1987/88 marketing year. However, EEP wheat expenditures for the current year are likely to be less than $400 million.

The true impact of the EEP program is difficult to determine. One recent USDA study estimated that the program achieved a 10-30 percent "additionality" effect for U.S. wheat exports. The oligopolistic structure of the world wheat market (a few large sellers) makes it likely that a price discount by one country will be matched by its competitors. The situation of the U.S. might be analogous to that of one of the Big Three U.S. auto makers. When one of these auto companies initiates a rebate program, it often finds that its competitors match its program with sales incentives of their own.

Price discounting is believed to be a phenomena of markets which are suffering from bulging inventories or excess production capacity. If we extend this analogy to the world wheat market, we can begin to understand why EEP subsidies have shrunk so much in the last year. As world wheat stocks declined, the wheat market shifted from a buyers' market to a sellers' market. If the major exporting countries increase wheat production and their stocks rebuild, we are likely to see a shift back to a buyers' market and a return to price discounting sales strategies.

The Case For A More Flexible Stocks Management and Continued Production Controls

If the USDA intends to continue in its "pro-active" management posture, a case can be made for a more flexible stocks policy and continued production controls. The importance of a flexible stocks policy can be illustrated by examining an episode that occurred about two years ago. At that time, strong world wheat demand combined with aggressive EEP initiatives, resulted in a 60 percent jump in U.S. wheat exports. In turn, this created a sharp increase in the need for "free" wheat, which was not available.

In order to meet this expanded export demand (and to keep subsidy costs within reasonable limits) the USDA began (in November 1987) to auction CCC owned wheat inventories. Until this time, the CCC could not make "sales" of its inventory unless market prices rose above the CCC's release price of $4.60/bushel. However, unless additional wheat was quickly made available, the EEP program would have to be curtailed or domestic prices would rise to higher levels. In order to increase "free" wheat supplies, the USDA chose to auction off some of the CCC's wheat inventory in exchange for generic payment-in-kind (PIK) certificates. The USDA's lawyers determined that, technically speaking, the auction was an exchange of assets, not a sale for cash. Even with these additional supplies, the EEP wheat subsidies that year were relatively expensive, averaging about $1.00/bushel.

The auctioning of CCC wheat is often facilitated by a manipulation of the premium that can be earned by purchasing CCC wheat with PIK certificates. The USDA has discounted (by as much as $.28/bu.) the price of its wheat inventory, relative to the market price that prevailed at the time. These substantial PIK discounts also gave producers a strong incentive to redeem grain stored under the Regular and Farmer-Owned Reserve loan programs.

At present, the quantity of wheat in CCC inventory, Regular Loan and Farmer-Owned Reserve is very small. Furthermore, if U.S. wheat stocks do rebuild over the next few years and farmers are permitted to put wheat into the Farmer-Owned Reserve, that would significantly reduce the USDA's ability to respond to changing market conditions. In turn , this could increase price volatility.

Once wheat is placed in the Reserve it tends to stay in the Reserve. Furthermore, there is no longer any "call" price mechanism which can be used to force producers to redeem wheat. Even if there were provisions that compelled farmers to redeem Reserve wheat when market prices rose to the Reserve's trigger, other aspects of the operation of the Reserve contribute to market instability.

When first introduced, the Farmer-Owned Reserve was designed to complement the 9-month Regular Loan Program. The intent was to construct a narrow corridor in which wheat prices would be permitted to vary. The Reserve's release price would act as the ceiling to market prices and the Regular Loan rate would serve as the floor. This "corridor" remained relatively narrow until the loan rate was sharply reduced in 1986. What had been just an $.80 corridor during the 1983/84 marketing year has widened to over $2.00 today.

If the USDA is going to continue to "manage" the U.S. wheat economy, any attempt to increase "free" wheat supplies to meet unexpected demand will be very difficult unless:

- the Reserve's trigger price is changed to a mandatory "call" price and this price is brought down to a level that permits farmers with grain in the Reserve to repay their loan and accrued interest charges plus some "premium" (ie. $.25/.50 bushel above total redemption costs);

- the Reserve is eliminated and any long term storage is accomplished by any of the following mechanisms:
  a. expired Regular Loans are forfeited to the CCC which is then free to "auction" these stocks for PIK certificates when market conditions warrant;
  b. expired Regular Loans are given one-year extensions but there is still a rigidly enforced "call" price which would be based on redemption costs plus a "premium";
  c. instead of a "call" price, storage payments are suspended and Pik-N-Roll incentives are increased to encourage redemption.

If the question of an appropriate stocks release mechanism can be resolved, there remains the matter of the "optimal" size of these stocks. The determination of "optimal" stocks levels is extremely difficult. Once a stocks program is created, there is a tendency for stocks to grow beyond any reasonable requirements. If a stocks program is available to absorb overproduction, farmers and policy makers become reluctant to accept the discipline of the market.

The demand for wheat is relatively inelastic with respect to its own price and, as a consequence of this, wheat prices may have to fall to very low levels to encourage additional consumption. If there was no loan rate (or if there was a "true" wheat marketing loan) wheat prices would fall to or below corn prices, in years of overproduction. In other words, to avoid building wheat stocks, excess production would have to be fed to livestock.

Excess stocks (beyond the requirements needed for an "optimal" inventory), would depress wheat prices and this would increase federal expenditures. Therefore in order: (1) to avoid pressure to let stocks grow beyond optimal levels; (2) to prevent wheat prices from falling to low levels; and (3) to keep deficiency payments at politically acceptable levels; production controls will be required.

A Word about the Normal Crop Acreage Proposal. It has been proposed that farmers be assigned a Normal Crop

Acreage (NCA) based on their farms' current base for program commodities plus their historical plantings of selected non-program crops. A farmer would be free to plant his total permitted acreage to any of a number of different crops and would still receive the deficiency payments that might be paid for his program crops.

For most of the last 10 years, the large majority of wheat farmers have participated in the government's set-aside programs. Forecasting wheat prices was simplified since U.S. wheat plantings were constrained by the size of the set-aside. Under the NCA proposal, farmers would, presumably, plant the crop which they believed would generate the highest expected net cash income per acre. In the Soft Red Winter wheat producing states (the Cornbelt, the Southeast and the Delta), corn, cotton, rice and soybeans would compete for what had formerly been exclusively wheat acreage. In the Plains and Pacific Northwest, corn, barley, oats, grain sorghum, sunflowers and rapeseed would be possible substitute crops. If, wheat farmers are suddenly freed of planting restrictions, what crops will they plant?

Some economists argue that farmers will evaluate current and expected market fundamentals and be able to forecast relative crop prices with reasonable accuracy.

Consequently, wheat farmers will, on average, plant just enough acreage to each crop so that there is no pressure to overproduce any single crop. This is a difficult theory to test since wheat producers' past planting decisions were so closely constrained by government programs. However, there is some evidence that wheat farmers planting decisions may be based on "naive" (no-change) price expectations.

Each year wheat producers in North Dakota are free to plant their wheat base either to Durum or to Dark Northern Spring (DNS) varieties. These producers are guaranteed the same wheat deficiency payment, regardless of which type of wheat they plant. An analysis of historical Durum plantings reveals that North Dakota wheat producers switch into-and-out-of Durum acreage based on last years' relative Durum and DNS prices. There is a pronounced tendency for Durum acreage to go up after years of high relative Durum prices and go down after years of low relative prices. In some years, Durum prices would fluctuate wildly in response to this back-and-forth planting pattern.

Introductory economics texts refer to this type of market instability as a "cobweb" market. The dominant characteristic of a "cobweb" market is wide supply swings which result in prices that range first above then below the "true" market equilibrium. Over time, these supply and price changes trace a pattern around the longterm market equilibrium which looks much like a spider's cobweb.

If, under the NCA proposal, all wheat producers made their planting decisions in a similar manner, this could introduce an substantial degree of market instability. This instability would creat an even greater need for a responsible and flexible stocks policy which could absorb "excess" production in years acreage was overplanted and then release those stocks in years when acreage was underplanted.

Conclusion

In the last five years the USDA, with the help of crop problems in the U.S. and other major wheat producing countries, has been able to eliminate a huge wheat surplus. This has contributed to a dramatic increase in wheat prices. To effect this amazing transformation, the USDA employed a number of new and not-so-new policy instruments to reduce production and stimulate export demand. In the process the USDA's top administrators have acquired some valuable skills in the "micro-management" of the nation's wheat economy.

These skills may be sorely tested in the next five years. The International Wheat Council is forecasting a record world wheat crop for 1990. Export demand for much of the last five years has been volatile but has not grown beyond the levels established in the early 1980's. Despite massive annual set-asides and the retirement of over ten million acres of wheat base in the CRP program, it seems that the U.S. has again borne most of the burden of adjusting to the changes in the world's wheat situation.

Economic reforms in Eastern Europe and the Soviet Union, if successful, may make these regions self-sufficient in wheat production. Many Latin American countries are saddled with huge debt burdens and/or chaotic domestic economies. The one bright spot in the demand picture is the impressive growth in wheat consumption in the Asian markets. Despite the expenditure of over $2 billion on EEP subsidies, it is unclear how effective the program has been or will likely be in the future. Although there may yet remain hope for meaningful progress in the GATT talks, I do not anticipate that the production or trade policies of the major GATT wheat exporting and consuming countries will be substantially altered in the next several years.

If total world wheat trade stagnates and the USDA intends to continue it's "pro-active" management practices, flexible stocks management mechanisms and continued production controls will be required. Furthermore, the Normal Crop Acreage proposal has the potential to introduce a significant new source of market instability. This instability can be managed, but only if the USDA is able to identify an "optimal" stocks level and can then fine tune production controls to prevent the acquisition of excessive inventories.

Senator **Boren**. We will now move to our panel of producer organizations: Reggie Wyckoff, past president of the National Association of Wheat Growers, from Genoa, Colorado; Louis Schupbach, president of the Oklahoma Wheat Growers Association; and Frank Dilse, vice president of the North Dakota Grain Growers Association.

We are happy to have all of you, and Mr. Wyckoff, I might ask, if you wish, just to summarize your testimony and we will put your full statements into the record and then we can go into any questions that it might generate. And fill free if you wish also to alter what you intended to say based upon what you have heard from our earlier witnesses.

STATEMENT OF REGGIE WYCKOFF, PAST PRESIDENT, NATIONAL ASSOCIATION OF WHEAT GROWERS, GENOA, CO

Mr. **Wyckoff**. Thank you. Let me just thank you for the opportunity. We tried to do this several times through the past summer.

PLEASED WITH THE 1985 ACT

I think that we as the National Association of Wheat Growers (NAWG) are pleased with the 1985 act and we would like to see its program design continued in the new legislation.

NAWG SEEKS TO RETAIN THE TARGET PRICE PROGRAM

The NAWG seeks to retain the target price program, and we hope that the Congress will reverse the declining path of income protection. We would also like to see target levels linked to unpaid acreage set-aside levels: so as the set-aside increased, so would the target price. This mechanism would assure stable income protection while also discouraging the announcement of excessive acreage reduction levels if the primary motive is to reduce potential Government outlays.

LOAN RATES

The NAWG supports the basic loan rates and formula setup in the 1985 act and we encourage the continuation of this policy. Loan authority should be used in a manner that will maximize returns to growers, and that portion of deficiency payments which results from the loan reductions should not be included in the producer's payment limitation.

WE WANT TO REGISTER OUR STRONG OPPOSITION TO PROPOSALS TO FURTHER LIMIT FARM INCOME BENEFITS TO PRODUCERS THROUGH "TARGETING"

In this regard, we want to register our strong opposition to proposals to further limit farm income benefits to producers through "targeting." Restricting eligibility based on a gross or net income test would be unfair and damaging to all farmers, while simultaneously destroying the operation of programs designed to assure adequate supplies of farm commodities for United States and foreign consumers.

THE NAWG WOULD ALSO LIKE TO SEE A PRODUCER-HELD GRAIN RESERVE MAINTAINED, BUT NOT AT THE HIGH LEVELS OF THE PAST DECADE

The NAWG would also like to see a producer-held grain reserve maintained, but not at the high levels of the past decade. A wheat reserve of about 300 million bushels would be adequate to provide market security, and its use should be linked to market signals.

WE DO NOT AGREE WITH THE PLAN ADVANCED BY USDA

We do not agree with the plan advanced by USDA, which we believe could allow reserves to be depleted before market prices reach target price levels. The USDA's proposal would also give the Secretary of Agriculture discretion to stop producer storage payments when prices reached just 140 percent of the loan level, or $2.59, and it would allow the Government to sell its grain into the market when prices reached only 110 percent, or $1.93 of the loan. The reserve must be a fluid reserve that gives the producer incentive to hold stocks and gives him the opportunity to move the reserve into the marketing channels when market signals are given. During the period the reserve is in release, producers should no longer earn storage payments, and interest charges should begin at some point to encourage the producer to move the reserve into the marketplace.

PRODUCERS SHOULD BE ALLOWED TO ROTATE STOCKS 60 DAYS PRIOR TO CONTRACT DATE

In an effort to ensure quality of grain placed in the reserve, producers should be allowed to rotate stocks 60 days prior to contract date. Delivered stocks must be required to meet the same grade and class as when entered into the reserve program.

FLEXIBILITY SHOULD BE PURSUED WITH CAUTION

Flexibility is the obvious theme of the 1990 farm bill debate, but we are suggesting this goal be pursued with caution. Many wheat farmers do not have economically or agronomically viable alternative crops.

Farmers should have the freedom within farm programs to respond to market needs or to change crops due to weather, conservation or disease problems. But flexibility should neither be used as a means of decreasing the safety net under farm income, nor should it be used to allow the artificial shifting of established program crops into different regions.

RECOMMENDATION

We recommend that new farm legislation should provide that the adjustment of any crop base for any farm for any crop-year, not to exceed 15 percent of the farm acreage for such farm for such crop-year. Program yields should be based on a 5-year moving average.

FEDERAL CROP INSURANCE PROGRAM

The administration has proposed that the Federal Crop Insurance Corporation's insurance program be terminated and it be replaced with a catastrophic Government disaster program. The catastrophic Government disaster program would be far less helpful than the special programs which were available for 1988 and 1989.

WE MUST MAKE SURE THAT AN INSURANCE PROGRAM IS AVAILABLE FOR THE 1991 CROPS

We feel that the Federal crop insurance program can be successfully redesigned. It also should be pointed out that as we work toward this goal we must make sure that an insurance program is available for the 1991 crops. Signup for the farm bill seeded crops will close this September and the insurance industry will need to know before this summer whether or not they will be able to offer multiperil insurance.

TRADE BILL

Mr. Chairman, the thing that I can say about the trade bill, I think that you are fully aware of our position on that. The most important thing I can say is use those trade tools aggressively, and we need to sell, not store, wheat.

ENVIRONMENT

The final broad category that I would like to address today is the environment. The conservation title of the 1985 act marked a major shift by merging, for the first time, farm program policy and environmental policy. The sodbuster and swampbuster provision of that title are worthy goals—and are workable when tied to the basic realization that conservation plans must also be economically feasible. The Department's alternate conservation system is a prime example of balancing our conservation goals with economic reality.

Already farmers are weighing the benefits of participation in farm programs against the cost of conservation compliance. This is important to note because there are many people within the environmental community that would like to tie program benefits to some form of environmental plan. We believe that many farmers will find such a carrot-and-stick approach to addressing environmental concerns too much stick and too little carrot.

Instead of placing more strings upon program participation, we should revamp our existing delivery system for addressing problems within agriculture. A renewed commitment toward research and education will ensure that those of us within agriculture can address concerns about chemical and fertilizer use and its effect upon ground water, the environment, and food safety. A concerted, united effort by the agricultural community toward addressing chemical use issues through improved management practices and enhanced education will preclude the need for regulatory solutions to environmental problems.

Thank you, and I would be glad to answer your questions.

[The prepared statement of Mr. Wyckoff follows:]

Statement of Reggie Wyckoff, Past President
National Association of Wheat Growers
before the
Subcommittee on Agricultural Production and
Stabilization of Prices
of the
Senate Committee on Agriculture, Nutrition & Forestry
on the 1990 Farm Bill
March 8, 1990

Mr. Chairman and Members of the Subcommittee:

Thank you for this opportunity to present the views of the National Association of Wheat Growers regarding the 1990 Farm Bill. I am Reggie Wyckoff, past president of the NAWG. My family and I operate a wheat farm near Genoa, Colorado.

Mr. Chairman, wheat growers are generally pleased with the way that the 1985 Farm Act has operated, and they would like to see its program design continued in new farm legislation. At the time that the 1985 Farm Bill was being written, the U.S. held a record inventory of wheat (1.9 billion bushels) and prices were seriously depressed. Now, five years later, stocks are projected to be at the lowest level in 15 years (468 million bushels), representing a decline of about 75 percent during the life of the 1985 Act.

The NAWG seeks to retain the target price program, and we hope that the Congress will reverse the declining path of income protection which began under the 1985 Act. We would also like to see target levels linked to unpaid acreage set-aside levels: so as the ARP increased, so would the target price. This mechanism would assure stable income protection while also discouraging the announcement of excessive acreage reduction levels to reduce potential government outlays.

The NAWG supports the basic loan rates and formulae set-up in the 1985 Act, and it encourages the continuation of this policy. Loan authorities should be used in a manner that will maximize returns to growers, and that portion of deficiency payments which result from loan reductions should not be included in the producer's payment limitation.

In this regard, we want to register our strong opposition to proposals to further limit farm program benefits to producers through "targeting." Fundamentally, farm programs can achieve desired national results because eligibility is almost universal and farming operations of all sizes can participate. Restricting eligibility based on a gross or net income test would be unfair and damaging to all farmers, while simultaneously destroying the operation of programs designed to assure adequate supplies of farm commodities for U.S. and foreign consumers.

The NAWG would like to see a producer-held grain reserve maintained but not at the high levels of the past decade. A reserve of about 300 million bushels would be adequate to provide market security, and its use should be linked to market signals.

We do not agree with the plan advanced by the Agriculture Department which we believe could allow reserves to be depleted before market prices reached target price levels. The USDA's proposal also would give the Secretary of Agriculture discretion to stop producer storage payments when prices reached just 140 percent of the loan level, and it would allow the government to sell its grain into the market when prices reached only 110 percent of the loan. Our policy calls for reserve wheat to go into release status when the average market price reaches 120 percent of the target price. During the period the reserve was in release, producers would no longer earn storage payments and would begin incurring interest charges.

In an effort to ensure the quality of grain placed in the reserve, producers should be allowed to rotate stocks 60 days prior to the contract date. Delivered stocks should be required to meet the same grade and class as when entered into the reserve program.

Flexibility is the obvious theme of the 1990 Farm Bill debate, but we are suggesting this goal be pursued with caution. Many wheat farmers do not have economically or agronomically viable alternative crops.

Farmers should have the freedom within farm programs to respond to market needs or to change crops due to weather, conservation or disease problems. But flexibility should neither be used as a means of decreasing the safety net under farm income, nor should it be used to allow the artificial shifting of established program crops into different regions.

We recommend that new farm legislation should provide for the adjustment of anv crop base for any farm for any crop year, not to exceed 15 percent of the farm acreage for such farm for such crop year. Any upward adjustment in a crop base must be offset by an equivalent downward adjustment in one or more other crop acreage bases established for the farm. Program yields should be based on a moving five-year proven yield determination.

The Secretary of Agriculture has proposed that the Federal Crop Insurance Corporation's insurance program be terminated with the 1991 crop, and that it be replaced with a catastrophic government disaster program. Under this proposal, government disaster assistance would be available only in a county that was declared a disaster, and the terms would be far less helpful than the special programs which were available for 1988 and 1989.

We feel the federal crop insurance program can be successfully redesigned. It also should be noted that as we work towards this goal, we must make sure that an insurance program is available for 1991 crops. Signup for fall seeded crops will close this September, and the insurance industry will need to know before this summer whether or not they will be able to offer multiperil insurance.

The Food Security Act of 1985 marked a major policy shift toward a more competitive, export oriented farm policy. The cornerstone of our export policy has been the Export Enhancement Program. The program has been used to accomplish three objectives: to compete with unfair trade practices in other countries; to increase exports of farm commodities; and to enhance our bargaining position in the Uruguay Round of Multilateral Trade Negotiations.

In the past four years, EEP has resulted in over $8 billion in sales of farm products, including 60 million tons of wheat and 2.7 million tons of flour. In the eyes of most wheat producers, the success of the program is without question: since the initiation of the program in 1985, the U.S. share of the world wheat and flour market has increased from 29 percent in the 1985/86 marketing year to 42 percent in the 1988/89 marketing year.

The final broad category that I would like to address today is the environment. The conservation title of the 1985 Act marked a major shift by merging, for the first time, farm program policy and environmental policy. The sodbuster and swampbuster provision of that title are worthy goals — and are workable when tied to the basic realization that conservation plans must also be economically feasible. The Agriculture Department's Alternate Conservation System (ACS) is a prime example of balancing our conservation goals with economic reality.

Already farmers are weighing the benefits of participation in the farm program against the cost of the conservation compliance. This is important to note because there are many people within the environmental community that would like to tie program benefits to some form of environmental plan. We believe that many farmers will find that such a carrot-and-stick approach to addressing environmental concerns will be too much stick and too little carrot.

Instead of placing more strings upon program participation, we should revamp our existing delivery systems for addressing problems within agriculture. A renewed commitment toward research and education will ensure that those of us within agriculture can address concerns about chemical use and its effect upon groundwater, the environment, and food safety. A concerted, united effort by the agricultural community toward addressing chemical use issues through improved management practices and enhanced education will preclude the need for regulatory solutions to environmental problems.

Mr. Chairman, members of the subcommittee, I thank you for the opportunity to testify. I will be pleased to respond to questions at the appropriate time.

Senator **Boren**. Thank you very much. I think that is excellent testimony. I share your concern about the crop insurance proposal, especially when you read the fine print. It is help that is really not going to be there in the case of many emergencies, if you have to meet both a per farm and per county test, if your farm is unlucky enough to be located in an area where it gets wiped out but not in a county that gets wiped out. I know our hailstorms are not always county-wide, for example, so you have a real problem there.

And I understand what you are saying about flexibility. So it would be the position of NAWG that it is worth experimenting with flexibility but you would hold it down to a 15 percent limit on the farm base?

Mr. **Wyckoff**. That is what our membership has felt, is limit it some. But as you know, the Secretary has had authority all the way through the 1985 act to do base substitution, but he has chosen not to. But he would be required to.

Senator **Boren**. Right. Thank you very much, those are very helpful suggestions.

Mr. Schupbach, glad to have you here today.

STATEMENT OF LOUIS SCHUPBACH, PRESIDENT, OKLAHOMA WHEAT GROWERS ASSOCIATION, ALVA, OK

INTRODUCTION

Mr. **Schupbach**. Mr. Chairman and members of the Senate Agriculture Committee, thank you for this opportunity to testify on issues concerning interests Oklahoma wheat producers have in the Food Security Act of 1990.

I am Louis Schupbach, a wheat producer and cattleman from rural Alva in northwest Oklahoma. I am presently serving my second term as president of the Oklahoma Wheat Growers Association (OWGA), the producer organization that represents Oklahoma's largest cash crop.

Besides this oral testimony, I have submitted a more lengthy effort in writing that I hope you, and particularly the media represented here, will all take time to read.

I would like to say that we do not believe the 1985 farm bill was successful, and considering time limitations allowed for these hearings, however, I will quickly itemize what amounts to OWGA's Christmas or wish list. I will be more than happy to answer whatever questions I can.

WHEAT PROGRAM PROVISIONS

TARGET PRICE

The OWGA board of directors has voted to support a wheat target price of $4.38 per bushel, or USDA's cost of production figure plus 15 percent, whichever is greater.

INCREASED ALLOCATION FOR AND USE OF EEP AND OTHER EXPORT SUBSIDIES

On increased EEP, while we are under the illusion that the EC, Japan, or any other major importing or exporting nation will abandon national food production goals, we support increased funding of the Export Enhancement Program and other international trade supports. It will be necessary to have those supports if we expect to compete even in today's market environment.

We would encourage the Secretary of Agriculture to more aggressively use EEP money that has already been appropriated. I would also like to add that the Southern Plains Winter wheat prospects are very good and we would like to see real aggressive use of EEP to get rid of this old wheat, old year wheat.

COMMODITY LOAN RATES

OWGA would like to see a loan rate of at least $3 per bushel.

RESERVE AND SUPPLY MANAGEMENT

OWGA believes that for national security reasons the United States should keep a comfortable grain reserve. Whatever the amount of the reserve is, it should be tied up for the exclusive purpose of supplying emergency food needs. Therefore, OWGA suggests releasing the reserve only after the commodity price reaches a parity level. In the case of wheat, approximately $7.65 per bushel. The national reserves should not be used as a market control tool, as has been the case since 1988 when USDA began issuing Commodity Credit Corporation stocks into the market to depress the price of farmer-owned and other free stocks. This practice, as is the case of the corn catalog recently issued, puts USDA in the position of operating as a national grain board and the objectives of USDA have obviously been adverse to farm profits. We also believe the mechanism of an acreage set-aside should be used to maintain stocks within a target range in excess of the established reserve.

Once again, we do not like the market effects of the 1.9 billion bushel wheat carryover, but it is obvious that millions of lives have been spared and made easier over the past 3 years because the United States built up the excess. We would encourage the United States to promote an international agreement to maintain a global energy food inventory.

FEDERAL CROP INSURANCE

We do not believe the administration's proposal to eliminate Federal crop insurance and turn exclusively to a disaster program is in the best interest of agriculture. As we understand the proposal, it does not address localized or fringe disaster, but farmers would qualify for assistance only if a disaster affects a majority of any given county. Injury suffered by local flooding, strip hailstorms, pocket drought or any other such malady that did not affect the entire county would have risk without remedy. Our study suggests that Federal crop insurance can be made a viable program.

PROGRAM CROP FLEXIBILITY

Areas in the Western Plains and the Southwest such as Oklahoma are limited in what they can grow for cash crops. Wheat is about the only viable commodity that does well in these regions. Therefore, program crop flexibility could do injury to our economic infrastructure, but there is very little good that it could do. If wheat markets would happen to improve to the point that wheat production was a profitable enterprise, areas with more versatility could enter the market and would eventually drive prices back down. OWGA would consent to flexibility of no more than 10 percent of program base, but it is doubtful that even that would be profitable in the Great Plains .

HAYING AND GRAZING

Cattle go with Winter wheat like butter goes with bread. Most wheat producers in the Western Plains and the Southwest are also cattle ranchers. In fact, without income from cattle during the latter 1980's, bankruptcy lines would have been considerably longer. Haying and grazing are important aspects of farm income for Winter wheat producers, so we believe both provisions should be written in the 1990 act. Please refer to my written testimony for a more thorough discussion on the subject.

ENVIRONMENT AND CONSERVATION

This is the one area where we support the administration's proposal for increased funding for research and education. Farm families live on the land from generation to generation, so we are as concerned as everyone else about preserving it, but we do not want to see unsubstantiated rules that restrict prudent use of fertilizers and agrichemicals, and we don't believe it is in anyone's best interest if farmers get stuck with the total cost of environmental and conservation requirements.

Thank you for the opportunity to speak on these important issues.

[The prepared statement of Mr. Schupbach follows:]

OKLAHOMA WHEAT GROWERS ASSN.
1512 Queens ∞ Ponca City, OK 74604 ∞ (405) 762-6942

March 8, 1990

Senate Agriculture Committee
United States Senate
Washington, D.C.

Mr. Chairman and Committee Members:

It is a great pleasure to have the opportunity to present testimony concerning farm interests in the Food Security Act of 1990, which will determine national agricultural policy through 1995. It is a hallmark of the American system, and a credit to you as our current elected officials, that you preserve the right of ordinary citizens to speak to issues of national importance.

My name is Louis Schupbach. I am a wheat farmer and cattle rancher from rural Alva in northwest Oklahoma. I am presently in my second term as president of the Oklahoma Wheat Growers Association, the producer organization that represents Oklahoma's largest cash crop.

As I prepared to come to this hearing, I felt that I should be able to speak to the issues of farm legislation and farm policy in general as a reasonably well informed citizen. One of the items that I attempted to digest was an article written by Texas Representative Dick Armey, one of the legislators who speaks for what I will call the extreme right in economic thought. While the statement the article makes does not come from President Bush, Secretary of Agriculture Yeutter or any member of the current or immediate past administrations, I am using it as a backdrop for preliminary statement of my testimony because it articulates the general philosophy of present and past administrations. The title of Representative Armey's article is "Moscow on the Mississippi: America's Soviet-Style Farm Policy."[1]

Representative Armey, who claims to have been a professor of economics in his pre-Washington life, in many ways exemplifies what United States agriculture, petroleum, mining and manufacturing industries, along with labor, have been confronted with throughout the past decade. He would have a laissez-faire economic system for everyone, farmers included. At the conclusion of his article, he shares Armey's Axiom No. 1, which he claims to have taught students when he was yet an economics professor: "The market is rational; the government is dumb."

I don't intend to dwell at great length on particulars in the discourse; hopefully many of you have read it, but I would like to point out that the pure laissez-faire system almost totally nullifies issues of sovereignty and what we might call the common good. Even with these differences of opinion, however, the article provides an excellent guide for a number of considerations that should be included in current and future national farm policy.

Possibly one of the greatest omissions of Representative Armey's article is the fact that despite supposedly new global politics, which the Representative romantically slips in under the Soviet term "perestroika," no industrialized or communist nation other than the United States has abandoned the goal of food self-sufficiency. The United States alone politically supported policies that caused the exodus of tens of thousands of family farmers during the 1980s.

Where the United States spent in the neighborhood of $15 billion for farm supports and export subsidies in fiscal 1989, the European Economic Community spent nearer $26 billion, thus demonstrating the EC's continuing resolve to preserve food self-sufficiency through a broadly based production system that avoids the problems that would certainly arise should the body politic and the citizen at large become dependent on a monopolistic handful of corporate producers. The last act before the Japanese Parliament adjourned in January was passage of the domestic subsidy for their rice producers.[2] And just this year, the Soviet Union will begin paying foreign currency cash bonuses to collective farms that exceed production quotas.

Last fall at the Geneva meeting of the General Agreement on Trade and Tariffs talks, EC and Japanese trade representatives the same as told the American trade team to take a hike with its proposal for deregulation of global agricultural production and trade.[3] And they have been true to their word. European farm producers continue to be supported, and, as already mentioned, the Japanese farmer is being supplemented at a level which permits him to stay on the land and produce at least the staples necessary to provide Japan with minimum food security without critical dependence on foreign suppliers, whether the United States or anyone else.

The United States, beginning in the 1940s, labeled the bill we are discussing the Food Security Act for basically the same reasons that the Europeans, Japanese and Russians all continue to strive for food self-sufficiency. Farmers, particularly in the United States but also in Europe and Japan, are a clear minority, but the food we provide our respective populations is the cornerstone of domestic tranquility and therefore political stability. The nation as a whole is at risk when and if the food production system breaks down, particularly if there are widespread economic woes threatening the rest of the cohesive and dependent system or if there are external conflicts that intrude on import supplies. We have not yet achieved Utopia or a sublime state of international cooperation.

Some of you have been in government over the past two decades so you will recall the 1970s OPEC oil embargoes. Prices skyrocketed. They affected the entire national economic infrastructure. As prices for petroleum fuels, chemicals, fertilizers and other products soared due to a monopolistic, short-supply market, inflation raced out of control.

We had a boom in agriculture in the 1970s[4], too, and food prices escalated, but imagine for a moment what would have happened to our economy had food prices risen at the rate that petrofuels increased.

Every American in the United States, whether in the city or the country, is a customer of American agriculture. The situation is even more critical today because under two percent of the population is now directly involved with food production.

Let's imagine for a moment that we had a general crisis in food production similar to what happened to perishable commodities in Texas, Florida and Mexico during the two December arctic fronts. I can give you a single example that will demonstrate the point: Prior to Christmas, tomatoes cost 49 cents per pound in Western Oklahoma. By the end of January, the retail shelf price was $2.69 per pound, or an increase of nearly 550 percent in just under six weeks.[5]

Perishable produce such as tomatoes and other fresh fruits and vegetables are nutritionally optional. Commodities, however, supply the basic dietary needs of the general population, particularly when other food items are priced beyond their budgetary reach. And this is the reason that the United States government, from the 1940s through the 1970s, maintained commodity farm programs that would assure stability in the farm sector and still provide the American public with an abundant, affordable and healthy supply of food.

The lassiez-faire advocate insists that through the 1970s, farm programs were never as expensive as they have become in the 1980s. But he alludes to the idea that there were minimum farm supports. The difference between prior farm bills and the 1985 farm bill, however, is the level of the commodity grain loans that for all intents and purposes established national and global benchmark prices. These loan prices assured American farmers, as well as the government, reasonable returns from the market -- the government was not paying huge deficiencies nor in the maine were farmers living off of government checks.

Because there was a benchmark global price, many farmers chose not to participate in federal farm programs, but they still received the benefit of government-established minimum prices.

By lowering the loan price, and therefore the global market price, the Food Security Act of 1985 created dependence on deficiency payments. The consequence has been greater public expense, which peaked at about $26 billion, and over 90 percent grain farm participation in federal commodity programs.

Many urban legislators as well as urban citizens seem to be largely ignorant of the historical role farm policy has played in stabilizing American agriculture and thus assuring the American public the most abundant, least expensive food supply anywhere in the world.

The American public now spends between 11 and 13 percent of disposable income on food.[6] No other industrial nation spends below 17 percent, and some spend as much as 26 percent of disposable income on food. The citizens of backward and developing Third World, and those in most communist nations spend upward from 30 percent and most of them over 40 percent of disposable income on food. Moreover, the quality of our food is second to none.

Supply management critics suggest that the American public is getting skinned at the grocery counter because of artificially high food prices. In reality, the American public is not paying a parity price, even with a substantial tax bill, that will support sustainable agriculture and assure national food security into the future.

You as Senators, who periodically go to your constituents and ask them to vote for you, must view the Food Security Act of 1990, and the American GATT proposals championed primarily by Secretary of Agriculture Clayton Yeutter, not just in a present context, but in terms of future and long-term political stability. The day you have to explain that the American public is hungry and that rising food costs have set off a catastrophic chain of economic events because Congress dismantled the broadly based family farming system that gave America abundance, will be the day that perestroika visits Washington the same as it has visited Rumania, Poland, Hungary, Czechoslovakia, East Germany, and now republics in the Soviet Union.

Is it possible for Americans to be hungry? I would like to remind legislators that the 1987 wheat carryover was approximately 1.9 billion bushels, a staggering sum that was called a surplus and considered a national problem. Adverse global weather patterns, however, created greater need in importing nations, as well as reducing production in exporting nations, and for three successive years, the global consumption of wheat has been greater than production. USDA presently projects that we will have a 443 million bushel carryover at the end of the current marketing year.[7]

Over 75 percent of what we felt was an astronomical reserve has been consumed, yet between 300 and 400 million people in our shrinking world go to bed hungry every night. We need but one more poor harvest in one or more major production countries and the nutritional level in developed nations, including the United States, could very well be threatened, particularly for lower income citizens.

As an interlude, I might point out that many long term weather forecasters are now proposing that the United States has entered an extended weather pattern somewhat like that of the 1930s -- a period in which the United States suffered varying degrees of drought from approximately 1930 until 1941. There were years during that time when the United States actually had to import grains to supply domestic need. And, historically we know of other periods such as 1837 when there were flour riots in the streets of New York City because food prices more than doubled due to shortages.[8]

In the long term, the laissez-faire argument prescribes the market equivalent of what the evolutionists call the law of the jungle or the survival of the fittest. It could just as well be called Supply-Side Economics, ushered in by former President Ronald Reagan, or Trickle-Down Economics, devised in the 1920s by Treasury Secretary Andrew Mellon. And, as was the case in the 1920s, agriculture in the 1980s traveled a rugged path. Our plight early in the century was resolved only by the collapse and extended distress of the general economy -- the unregulated free market, as has more recently been the case for over-regulated, centrally planned economies, demonstrated vulnerability by way of failure and great human misery. The extremes travel opposite paths to arrive at more or less the same end.

I will make one more comment concerning the supposed rationale of the unrestricted, unregulated market, then offer suggestions which the OWGA board of directors support.

In the United States, the "rational market," which Representative Armey says is far superior to government, spends about $500 billion per year on illegal and harmful drugs. The rational moral market, if that is an appropriate term, is responsible for the epidemic spread of AIDS.

These two examples of unbridled market rationale, whether economic or moral, represent the dichotomy of human nature that imposes itself on all human intercourse. The market is not an entity unto itself, but it is a product of human enterprise, and as such, it manifests both good and bad. Had man been capable of living harmoniously, without regulation and precepts defining the common good, governments would never have been devised.

Wheat Program Provisions

The Oklahoma Wheat Growers Association board of directors voted to support a wheat target price of $4.38 per bushel or USDA's cost of production figure plus 15 percent, whichever is greater.

Leading agricultural economists, including the major association of university agricultural economists, project that even if 1990 target prices are stabilized at their current level, by 1995, net farm income for commodity grain producers will decline by 25 percent or more, and if target prices continue to be lowered, net farm income will fall by as much as 40 percent.

Many proponents of the 1985 Act argue that its provisions improved farm income. We do not feel that this has been the case. To begin with, most of the improvement came from livestock and other non-program sources. Secondly, net farm income improved because the farm community was forced to pay down debt rather than make purchases in the environment that has persisted since approximately 1982. This has resulted in devaluation of farm equipment and vehicles at a level that now exceeds $50 billion.

Thirdly, agriculture benefited by substantial declines in the cost of interest, fuels, fertilizers and other necessary non-equipment and non-land expenditures.

The probability of the same broad reductions continuing for another five years is at best remote. As equipment ages, more farmers will be forced to make new purchases or simply go out of business. Since spring 1988, we have seen interest rates reverse, and in the past year we have seen substantial increases in fuel, fertilizer and petro-based farm chemicals.

In short, sustainable production of commodity grains, wheat included, will be all but impossible with policy that does not recognize these essential production costs.

Increased Allocation For and Use of EEP and Other Export Subsidies

Grain export volumes will continue to depend on production conditions in importing and other exporting nations. It is clear that nations that can, fully intend to produce to levels of self-sufficiency, and the EC in particular appears to be resolved to supplemented full production programs. In order to market grains in the global trade environment that exists today, the United States will obviously have to supplement export sales. Fortunately, dollars created through the handling, transportation and marketing systems for exported agricultural products more than compensate for the tax expense.

It is worth noting that the 1985 Act was constructed with the EC as its primary target. Although we have increased our share of total grain exports, the EC has retained its share. Canada, Australia and other smaller nations have been hurt the worst. We should not be under the allusion that the Europeans are going to abandon their food production goals even as we pour money into export marketing.

I would also call attention to the role agricultural exports played in the 1989 American trade deficit: dollars earned from agricultural exports off-set growth in non-agricultural imports, and as a consequence, the 1989 American trade deficit was the lowest since 1984. It will be in the national best interest to continue support of strong agricultural export programs.

We would like to see USDA be more aggressive in the use of EEP funds presently available. Shipments of the 1989 wheat crop have for all intents and purposes been suspended, so funds are idle which could be used to continue marketing.

Commodity Loan Rates

Commodity producers cannot be classified with manufacturing and other types of business that set their own price to sell into wholesale or retail markets because we sell through what amounts to an auction system that is controlled by multinational and conglomerate corporations. Because the United States is the largest export grain producer and we usually hold the balance of the global reserve, the loan rate serves as the international benchmark price. Historically, when our loan rate is low, commodity prices are low. The floor we establish for commodities works somewhat the same in international grain markets as our fixed gold price did for international currencies from the mid-1930s to the early 1970s. Therefore, we would like to see the loan rate substantially increased.

Research into the concept of elastic pricing, which theoretically results in higher sales volume with lower prices[9], suggests that there is little or no validity to the notion. Where food is concerned, importing nations will purchase the amount of grain they need when they need it, and within reasonable limits, price has very little to do with when and how much they purchase. A loan price near or even above the target price would have the result of greater farm earnings from the market rather than from the government. This was the policy throughout the 1970s when the Soviet Union and China first came into international grain markets so there is no reason to think importing nations would act differently today than they did 15 to 18 years ago so long as prices aren't inflated beyond reach.

At the very minimum, OWGA feels the wheat loan rate should be increased to $3.00 per bushel. This is not an unreasonable floor for wheat. In November 1947, wheat sold at Oklahoma elevators for $2.87 per bushel. That was one of the few times that wheat reached what might be termed a parity price, and the cost of production certainly hasn't gone down in the last 40 years.

Reserve and Supply Management

If the farm community was concerned solely for its own best interest, we would just as soon see the national grain reserve sold out. During prolonged difficult growing periods, prices would soar. But we realized that economic and political stability is in our best interest, too. Therefore, we believe that a healthy reserve is necessary.

We would like to see Congress establish a reserve adequate to meet national and even modest export needs during critical periods that might cover two or more years. The reserve, however, should not be a tool available to hold down prices as Commodity Credit Corporation stocks have been since 1988.

In order to have the reserve and see to the national best interest, the trigger level for releasing reserve stocks should be at the parity price. This would avoid the situation we have today where wheat prices have been held down by the repreated issuance of CCC catalogs then the nation face the problem that one high-ranking USDA official has described as "dangerously low" wheat inventories. The reserve was originally intended to safeguard national food security, not to equip USDA as a national grain board, but this is precisely what has happened during the term of the 1985 Act. OWGA strongly opposes this kind of use of the grain reserve and believes that it should be locked in, whatever the amount, at a price level that will not affect markets during normal times.

Federal Crop Insurance

The Administration has recommended elimination of Federal Crop Insurance in favor of disaster payments. Unfortunately, the recommendation is based on countywide disaster and does not address localized or fringe disaster such as borderline catastrophe for farms adjoining disaster counties or limited-area disaster such as strip hail storms, local flooding or pocket drought. We feel that this is a substantial flaw in the Administration's proposal which Federal Crop Insurance addresses. Without crop insurance, the individual farmer would face risk without remedy.

Research I've done suggests that Federal Crop Insurance can be salvaged, particularly if there is more uniform adjustment and supervision between Federal Crop Insurance and privately administered multiperil policies. Both programs need to be put on am actuarially sound footing that is uniform and equitable.

Program Crop Flexibility

In Oklahoma, we today have llamas and ostriches. Unfortunately, markets for these critters are limited so not everyone has turned to exotics as a means of diversification. It appears, for the next few years at least, that wheat and beef will continue to be our financial bread and butter. To varying degrees, the same is true throughout most of the Great Plains and Southwest except where irrigation is available.

In concession to those who advocate flexibility for program crops, OWGA would consent to optional or alternative program crop planting on 10 percent of a farm's program base. At present, however, producers in arid regions probably could not benefit even from that. In fact, farmers in the corn belt could take advantage of the more lucrative corn deficiency payment, plant wheat as an alternative crop, and do us considerable economic injury.

For the past several years, the Agriculture Experiment Station has been experimenting with alternative crops that will grow in our exclusionary environment. We hope that in the next decade, we will have more alternatives, but for now we would prefer not to throw the flexibility door wide open as it could result in serious destabilization for our region.

Haying and Grazing

Winter wheat is a unique crop because it can be pastured through the winter and thus provide a source of diversified income. In fact, most wheat producers in Western Oklahoma and many other winter wheat states in the High Plains and the Southwest are also cattlemen.

When we have a wheat set-aside or prices are low, we can graze out or hay acres that are not going to be harvested for grain. Most wheat hay is kept on the farm so it is used by the original producer. When the pasture and/or hay is available, wheat producers tend to purchase more steers. This directly improves farm income and the economic climate of the rural community. Cow-calf operations, most of which are located in other regions of the country, find this a ready and profitable outlet which is healthy for them, too.

Dr. Daniel Bernardo at Oklahoma State University estimates that the average income for Oklahoma over the past ten years for November-to-March 15 pasturing has been around $56 million. Haying and pasturing poor stands, stands produced during down markets, and set-aside acres through the complete season would add substantially to and could even double this much-needed income.

Studies have also demonstrated that stocker cattle fed and conditioned on wheat pasture and wheat hay frequently have improved rates of gain once they are moved to feedlots for finishing. This translates to benefits across the board and we feel that haying and grazing rights should be written into the Food Security Act of 1990 as automatic program provisions.

Environment and Conservation

Nobody is more aware of the need for sane use of agrichemicals, fertilizers and other farm in-puts than farmers. For most farmers and ranchers, the land is precious because it is passed from generation to generation. As a consequence, we want to preserve and even improve the resource that provides our livelihood and will hopefully do as well or better for our lineage.

What we fear, however, is over-reaction to some problems that definitely need to be addressed. Radical reduction of fertilizers and agrichemicals could reduce farm productivity by 40 percent or more, and as a consequence, in the short term, farm income would decline, but in the long term, consumer food prices would soar. Therefore, it is in everyone's best interest to invest in research and education so we can find a manageable but satisfactory balance.

Our second concern in this area is that during a time when farm support programs are being targeted as budgetary evils, the farmer could be saddled with the costs of ecological restoration and management without compensation that will continue to support earnings. Already farm program participation has been tied to conservation compliance and in many cases this could yet be the straw that breaks the camel's back. OWGA would again encourage prudent consideration for long term farm and consumer needs when adding regulations that may appear expedient but could do permanent damage.

If land that is being defined as wetlands under today's regulations have been in production for five years or longer, or if the amount of land involved is under an acre, those lands should be exempted from existing conservation regulations. This is one of the areas where present legislation has approached throwing the baby out with the bathwater and we feel that this and some of the other current conservation regulations need modification.

Thank you for this opportunity to testify. I will be happy to answer whatever questions anyone cares to ask.

Sincerely,

Louis H Schupbach

Louis Schupbach
OWGA President

[1] "Moscow on the Mississippi: America's Soviet-Style Farm Policy," by Representative Dick Armey, Winter 1990 issue of "Policy Review."

[2] The Japanese are confronted on the one hand by aggressive American efforts to open their markets to international trade, and on the other by domestic pressure that demands greater attention to, and in some cases, more protection for, domestic interests. Concessions for the import of more American beef contributed substantially to the ire of many Japanese voters when the ruling party suffered severe loses in upper house elections last summer. The lesson wasn't lost. The ruling party returned a slim majority to the ruling lower house in February, but the Japanese people fired a clear enough shot across their bow that the probability of further concessions, particularly where agricultural trade is concerned, is pretty remote. This has set up a particularly difficult relationship between Japan and the United States which could result in considerable trade animosity in the trade arena.

[3] It should be remembered that the Montreal GATT talks in December 1988 broke down primarily because of the gunboat diplomacy of the American trade team, then led by Clayton Yeutter, serving as President Reagan's Senior Trade Advisor. Following that failed round of talks, the Europeans placed a ban on hormone-injected American beef, and through the early part of 1989, we skirted dangerously close to a trade war with the EC. When the American trade team went to the Geneva GATT meeting last fall, then led by Carla Hills, EC and Japanese representatives quickly set the agriculture issue aside, warning that if the United States continued to pursue the hard line there, to the exclusion of other considerations, everyone just as well pack up and go home again. Consequently, claims of progress toward laissez-faire agriculture trade are for the most part one-sided rhetoric coming from the Administration and there is very little basis in fact to support the idea that we will ever see completely deregulated agriculture trade in our lifetimes.

[4] The was the third major agriculture export period of this century for the United States. The first was during and immediately following World War I and the second during and immediately following World War II. The first two were due to the political disruptions of the wars and disturbance to food production systems that normally supplied nations involved in the wars. When China and the Soviet Union came into global grain markets in the early 1970s, there was political motivation there, too, as political leaders attempted to better supply domestic food demand during their years of adverse growing conditions. When production conditions improved, the volume of grains sold into the international markets shrank. See The Economic Structure of Agriculture: Rhetoric Versus Reality, by Dr. James Plaxico and Dr. Daryl Ray, Oklahoma State University, for a more thorough examination of these unique periods.

[5] These prices were watched at a Homeland grocery store in Ponca City.

[6] In the late 1970s, Americans also paid 15 to 17 percent of disposable income on food. Policy in the 1980s, however, has worked against farm interests, and while tax support for farm programs has increased, the consumer shelf price of food has been driven down, more than compensating the public for the sum spent on farm supports. Money freed from the American food bill, along with relief from spiraling energy costs, has been diverted to other areas of the consumer market, and as a consequence, the farm community, along with the oil patch and other base American industries, has paid a dear price for the prolonged 1982-89 urban economic recovery that today appears to be skirting its own crash.

[7] The current argument which supports the idea that the "supply pipeline" can operate efficiently with a lower reserve than the United States has maintained in the past is based on technical improvements in handling and transportation -- the supply pipeline, as it were, doesn't need the same "volume" to draw on to keep grain moving from farms and country elevators to processors and export terminals as was required in the past. The flaw in this reasoning, however, is the assumption that agriculture is like other industries. That is, there is an assumption that food is produced with the same dependability the industrial assembly line has. Unfortunately, it isn't. Adverse weather in December did enough injury to the tomato crop in winter growing areas that supply was far less than demand, so the commodity inflated by approximately 550 percent in about a month. We can expect the price of avocados and other California perishables to inflate because of a more recent cold front that dipped deeply into California. And, given another poor harvest in any of the grain-producing regions or countries, we can expect inflated grain prices. The grain reserve, then, is not simply to keep the "wheels of industry" turning, but to assure food and therefore economic stability.

[8] In his Oct. 21, 1989 issue of "The Browning Newsletter," Iben Browning writes, "Since I calculate each of the next two years to be the stormiest since the U.S. became a nation, I expect great crop losses in the U.S. and Canada. I expect the U.S. reserve to be completely used up in 1990, and another crop loss in 1991, with no reserve and premature slaughter of stock animals to save feed. I expect hunger in the U.S. and Canada in 1991 comparable to 1837 -- the year of the 'Flour Riots' in New York (prices doubled in 1937 in NY); and the two Rebellions in Canada..." Study of food cycles done by Louis Thompson, a professor at Iowa State University, tends to support Browning's position as Thompson projects a continued decline in food supplies until 1994. In the Feb. 17, 1990 issue of "Pro Farmer," half a dozen long range forecasting services are quoted as projecting varying degrees of difficulty through the first half of this decade. One of the forecasters notes that El Nino, the major ocean current that has been dealing Ethiopia fits with three droughts in the 1980s, is positioned to give the United States major difficulties at least through 1991 and '92. Several of the forecasters are comparing our weather patterns since approximately 1988 to those experienced in the 1930s -- with a few less severe years interspersed, there was drought beginning in 1930 that was not totally relieved until 1941. During the worst "Dust Bowl" years (the Northern Plains in the Dakotas were actually hurt worse than the infamous Okies), the United States actually had to import grains in order to supply domestic needs.

[9] See The Economic Structure of Agriculture..., Plaxico & Ray.

Senator BOREN. Thank you very much, Louis.

I gather both you and Reggie would—you heard earlier Dr. Gardner's statement that it was only an inside the beltway mentality that we might have some misgiving about going to 100 percent flexibility. I guess you would both find that there are widespread concerns among those with whom you have talked who would want us to start with an experiment, I think Louis said 10 percent, Reggie said 15 percent, but some sort of a cap on the level of experimentation that we would allow with flexibility here?

Mr. WYCKOFF. Mr. Chairman, I was in probably 10 of our 18 States this fall and in every State they spoke about the open ended of NCA.

Senator BOREN. They were concerned about an open ended flexibility.

And Louis, do you find the same thing in terms of Oklahoma producers?

Mr. SCHUPBACH. Yes. Now, I wouldn't be so sure—we are talking about program crop flexibility. Nonprogram crop flexibility I think most wheat growers in my State would be all for.

Senator BOREN. But not program crop flexibility?

Mr. SCHUPBACH. Right.

Senator BOREN. It would have to be within limits. Thank you very much. Mr. Dilse, glad to have you with us.

STATEMENT OF FRANK DILSE, VICE PRESIDENT, NORTH DAKOTA GRAIN GROWERS ASSOCIATION, SCRANTON, ND

Mr. DILSE. Thank you. I am pleased to be here. I will summarize my testimony.

DROUGHT

Our State is coming out of 2 years of drought. Most of the State, including the very productive Red River Valley, has yet to receive moisture recharge. It is very unusual for them to be short on moisture. I live in southwestern North Dakota, and we are usually the drier end, and I believe they are a lot worse off than we are right now.

TRANSPORTATION DIFFICULTIES

To top it off, we have been experiencing transportation difficulties this winter. At one point I went in to sell grain and you just about got laughed at. It was at this time I think the railroad was running about 87 days behind on car deliveries. Our local elevator at the high point was paying about $1,300 a day in interest on grain that they had sold and had been unable to ship. The livestock sector I think has picked up, but the grain sector has not in our State. We have not experienced the net income rebound that some sectors are enjoying. I guess our biggest priority is rain. Next to that I think is——

Senator BOREN. I wish we could help with that.

FEDERAL CROP INSURANCE

Mr. DILSE [continuing]. I do too. I think the next priority item to us at this point is Federal crop insurance. We are a high overhead, low margin, high risk form of business, and both the farmers and the bankers are very concerned about having an adequate program in place. I guess when you appointed the Commission to study Federal crop insurance, we had hoped that significant change would happen. It didn't. The zero budget for Federal crop insurance brings this to a head, and hopefully Federal crop insurance can be resurrected into a workable program.

Our association definitely favors restructuring of the Federal crop program over legislated disaster assistance. Our association favors——

Senator BOREN. What percentage of your people sign up for crop insurance in North Dakota, do you know?

Mr. DILSE. I believe we are probably one of the higher States as far as participation. I don't know the percentage for sure.

NDGGA FAVORS TARGET PRICE CONCEPT

The North Dakota Grain Growers Association favors the target price concept, but we are real concerned when we see projections of what our machinery and input costs will be in the future. I think they are talking over the next 10 years we are going to be looking at a 50 percent increase. When our inputs are going up like everyone else's and the target price is trending down, it makes us nervous.

NDGGA SUPPORT A FARMER-HELD RESERVE

The North Dakota Grain Growers support a farmer-held reserve with storage payments comparable to commercial rates, and we also support provisions to allow for rotation of these stocks to ensure preservation of quality.

EEP

We support the Export Enhancement Program.

SODBUSTER/SWAMPBUSTER PENALTIES

We feel strongly that the penalties of sodbuster/swampbuster should come more in line with the severity of the infraction.

The Grain Growers Association feels that Mr. Scaling, Chief of Soil Conservation Service, and his staff should be commended on completing a program of the magnitude that sodbuster/swampbuster was and bringing it in on schedule, but were it not for his allowing the alternate conservation systems, it would have been difficult to complete it on schedule and it would have been impossible for some farmers to comply with it.

I think what people have to realize is because of the size of that project most of those plans were completed without any Soil Conservation Service technicians ever visiting the farm. To work out workable plans, I think you have to have the on-farm inspections to get the plan to reality. Without the alternates, we would have had lots of troubles.

WE ARE STILL HAVING PROBLEMS WITH THE NUISANCE POTHOLES IN NORTH DAKOTA

We are still having problems with the nuisance potholes in North Dakota, and we have been working to try and get the class 1 nuisance potholes exempted from swampbuster coverage.

WHEN YOU HAVE A NEW SET OF REGULATIONS IMPOSED, IT CURTAILS FLEXIBILITY, AND THAT CONCERNS US

I guess I think it is ironic that this year the catch word of the new farm bill is flexibility, and yet of the things the environmental side that I hear coming in is it creates just the opposite. When you have a new set of regulations imposed, it curtails flexibility, and that concerns us.

CONCERNS

The weather and markets used to be our greatest concerns, and lately we have had to add regulation to those concerns. I feel food safety, ground water, and responsible chemical use are issues that we have always believed in. I feel that when you look at the definitions of LISA most farmers are already there. Chemicals are expensive. We do not use them unless we have to. If we can forgo a chemical we do. There seems to be a misconception that farmers are out there randomly dumping chemicals on their fields, and that is not the case.

It seems like we are also catching a lot of heat from the wildlife groups, and this kind of confuses me, because it's farmers that feed wildlife in the rough winters, and the farmers probably plant more trees than anyone else. There are excellent programs for the wildlife. Our State Game and Fish Department and organizations like Pheasants Forever have cooperative programs where farmers seed food plots and distribute winter food for wildlife. They have worked along with ASCS, and this land can be used for set-aside. Maybe we have done a poor job of PR or whatever, but it seems like a lot more could be accomplished with cooperation than with legislation in these areas.

We are quick adapters, and I urge you to help us solve our problems through education and cooperation, not with blanket regulations that attempt to solve specific problems.

Mr. Chairman, I thank your for allowing me to testify.

[The prepared statement of Mr. Dilse follows:]

PREPARED STATEMENT OF FRANK DILSE, VICE PRESIDENT, NORTH DAKOTA GRAIN GROWERS ASSOCIATION, SCRANTON, ND

Mr. Chairman and members of the subcommittee:

Thank you for this opportunity to present the views of the North Dakota Grain Growers Association (NDGGA). I am Frank Dilse, second vice president of the NDGGA. I have owned and operated a grain farm in southwestern North Dakota for the past 22 years. I raise wheat, durum, barley and sunflower.

Our State is coming off 2 years of drought. Most of the State, including the very productive Red River Valley, has yet to receive moisture recharge. This winter we experienced massive transportation problems. Our State is an area that has not experienced the net income rebound that some sectors are enjoying.

Because of our current situation, Federal crop insurance is of major importance to us. We are a high overhead, low margin, high risk form of business and we, as well as our bankers, are very concerned with the fate of Federal crop insurance.

In the past we have sought higher levels of coverage from Federal crop insurance. When you appointed the Commission to study crop insurance we were given hope that significant change would happen. Federal crop insurance being budgeted at "zero" brings the issue of disaster payments and crop insurance to a head. Hopefully crop insurance can be resurrected into a workable program.

We have been hearing about a catastrophic government disaster program that would be based on a county being declared a disaster. We feel this would not be a desirable option since drought, hail and insects do not recognize county lines. It is conceivable that I could lose my crops while the balance of the country was fine.

Mr. Chairman, the NDGGA supports a redesigned Federal crop insurance program.

The NDGGA favors the target price concept. However, because of increasing production costs we favor reversing its downward trend. The NDGGA also favors linking the target to an unpaid acreage set-aside. As acreage is taken from production, the target price would increase.

The NDGGA supports a farmer-held reserve with payments comparable to commercial rates. We also support provisions to allow for rotation of these stocks to ensure preservation of quality.

The NDGGA supports continued use of the Export Enhancement Program.

Mr. Chairman our association feels strongly that the penalties associated with sodbuster/swampbuster should come more in line with the severity of the infraction.

Mr. Scaling, Chief of the Soil Conservation Service (SCS) and his staff should be commended for completing a program of this magnitude on schedule. Were it not for the alternate conservation systems it might not have been complete on schedule. But it is still not without problems. Our association is still seeking to get an exemption for Class 1 nuisance potholes. This topic may not come directly under your committee oversight but it does affect a grain grower's ability to farm.

It is ironic that, while the catch word of the new farm bill is flexibility, just the opposite may be the case. Whenever a new set of regulation is imposed, it curtails flexibility.

Mr. Chairman, weather and markets used to be a farmer's greatest concerns. Lately we've had to add regulation to this. As a farmer I feel like I am under siege. The attack comes in areas that have always been of great importance to us. Food safety, ground water, and responsible chemical use are issues we farmers have always believed in. From what I see we are already LISA farmers.

It seems as if we are also under attack from the wildlife groups and this confuses me. Farmers are wildlife promoters. We are the tree planters of the Nation. There are programs through our State Game and Fish Department and through organizations like Pheasants Forever in which farmers seed food plots and distribute winter food for wildlife. And yet rather than working with us for better solutions, the wildlife groups would have you force legislation on us. I don't understand this. More could be accomplished by working together.

Farmers are quick adapters. I urge you to help us solve our problems through education and cooperation, not by intimidation and blanket regulations attempting to solve problems best resolved by cooperation.

Mr. Chairman, members of the subcommittee, I thank you for the opportunity to testify and will be pleased to respond to any questions you may have of me.

Senator BOREN. Thank you very much, Mr. Dilse. And let me say, as you could probably tell from the earlier conversation with Senator Conrad, your Senator forcefully brings forward many of the same points that you have brought forward in your testimony today as a member of this subcommittee. And he does it with great effectiveness, let me say.

Let me ask you, on the provision about flexibility-and by the way, I certainly agree with what all of you said about crop insurance, as you could probably tell from my comments, and in talking to several other colleagues on the committee, I think there is a real reluctance to accept the administration's proposal to simply zero out crop insurance.

Definitely there are improvements that need to be made in the system, and that is the reason we went through the Commission route and why we have been struggling to come up with the recommendations, but I think there is a strong consensus emerging, at least among the members I have talked to, to certainly not throw the baby out with the bath water, but to keep on having crop insurance and continue to struggle to improve the system we have rather than just doing away with it. So I think all three of you will be heeded on that point.

On the flexibility part, the total farm base, you have heard your two copanelists talk about a 10 or a 15 percent. How do you feel about the 100 percent proposal, the administration proposal?

Mr. **Dilse**. I guess that probably also makes me a little bit nervous. I can't equate yet if acreage would be shifted from one region to another or not.

I would like to add that in our area, when I left home Monday our grain price was $3.12 for 14 protein Spring wheat, and where our wheat is a premium wheat to use for blending, and because of the drought the Winter wheat came in with higher protein, adversely affecting our Spring wheat prices. Also the transportation problem has taken 8 or 10 cents off our prices.

With the contract crops, January, February is the time of year when they announce their contracts. With the high oleic sunflowers, when they announced those for our corner of the State, I think their contracted acreage was filled up in 4 days, confection sunflowers the same way. It was a week or so. With safflower, the elevator that contracts the safflower scheduled a set of meetings, and by the end of the second meeting their quotas were filled. There is going to be a big shift away from wheat in my area.

Senator **Boren**. You can see the real pressure for shifts under certain conditions like you are facing there.

Well, thank you all three of you.

Yes, sir, Mr. Wyckoff.

Mr. **Wyckoff**. Sitting here today, thinking about the full flexibility that they are talking about and the way that that is going to be run, it seems to me that there is something wrong in the logic of being able to plant wheat on a corn base and receive the corn deficiency payment. That doesn't sound right.

You know, it doesn't sound morally right to be having that. I think we need to take a cautious look at that and see what the implications are going to be before we accept something like that.

Senator **Boren**. I appreciate your comment. I appreciate the testimony all three of you have given and we will put your full statements into the record.

Thank you very much for being with us and thank you for your patience as we have run behind schedule.

Our concluding panel—and we will try to conclude as close to 5 o'clock as we can—Mr. Randy Marten, vice president for materials acquisition and transportation, Campbell Taggart Inc., Dallas, Texas; Mr. Stephen Goulding, president of Oak State Products, Inc., a baker of Archway Cookies on behalf of the Biscuit and Cracker Manufacturers' Association, from Wenona, Illinois; David Lyons, director, North American Export Grain Association here in Washington; and Mr. Duane Fischer, president and CEO of Scoular Grain Company, representing the National Grain and Feed Association, Omaha, Nebraska.

Let me say, we wouldn't have made these Texans and Nebraskans wait until last just out of pure perversity here.

If I had looked at this, we might have been more gracious, even in spite of their misbehavior certain days of the year.

Mr. Marten, why don't we begin with you.

STATEMENT OF RANDY MARTEN, VICE PRESIDENT, MATERIALS ACQUISITION AND TRANSPORTATION, CAMPBELL TAGGART INC., DALLAS, TX; REPRESENTING AMERICAN BAKERS ASSOCIATION, WASHINGTON, DC

Mr. MARTEN. Thank you. Good afternoon.

INTRODUCTION

My name is Randy Marten. I am vice president for materials acquisition and transportation for Campbell Taggart. I am here today on behalf of the American Bakers Association which represents companies that produce approximately 80 percent of the baked goods in the United States. We appreciate the opportunity to present the wholesale baking industry views before this subcommittee.

We wish to reaffirm our strong views on the need to reduce Government intervention in agriculture and to let farmers produce abundantly for markets at home and abroad. However, we recognize that maintenance of grain reserves and assurances of food safety require a governmental role. We know that the Government must respond when exports face unfair competition, but we feel that there can be less Government in agriculture while still carrying on these important and necessary activities.

FIVE KEY AREAS MOST IMPORTANT TO OUR INDUSTRY

Our position in five key farm program areas are as follows:

First, we seek adequate supplies of wheat and other products created by flexible programs.

We believe that the acreage reduction program for wheat should be phased out over time. If it is retained in the law, the program should be operated so as to maintain total carryover stocks at or near 40 percent of a year's needs for all purposes, including exports.

Farm programs should provide more flexibility for farmers to determine their cropping patterns on the basis of market signals. Shortages of oats and oilseeds could be avoided if acreage programs for wheat, corn and cotton were less rigid.

Consideration should be given to combining the farmer-owned reserve (FOR) and the food security wheat reserve, to minimize CCC ownership of grains. Shorter reserve contracts and lower release prices along the lines proposed by the administration may serve as a pattern for amending present law.

No wheat land should be added to the Conservation Reserve (CR) after 1989. The 11 million acres of wheat land contracted now have significantly reduced our capacity to produce wheat. We strongly urge the Secretary of Agriculture and Congress to delay any additional conservation reserve signup until after new criteria have been considered in the farm bill debate, possibly shifting the objectives of conservation reserve from soil erosion to environmental improvements.

Two, we favor price and income supports for farmers.

We believe that the present formula for adjusting loan rates from year to year based on average market prices in 3 of the previous 5 years is workable for the 1990's. Increases as well as decreases in actual loan rates should not exceed 5 percent per year, however. This will help ensure stable and competitive prices.

Three, export programs. We support reasonable operation of our export programs.

We support U.S. policies to ensure a strong competitive position in world trade. We agree that the Export Enhancement Program needs to be used in certain circumstances to meet competition from the European Community and other countries. However, the EEP needs to be operated with greater consistency and openness than in past years to minimize market surprises and the impact on farmers and bakers. Business-like use of export credit programs, and generous food aid programs, also have our support. We encourage grain quality improvements.

Four, grain quality. The 1990 farm bill should make development and production of high quality wheats that meet the needs of bakers and consumers in the United States and around the world a top priority. We strongly support increased funding for USDA and university research on grain quality. Specific proposals on grain quality were provided in testimony on February 22d before the Senate Subcommittee on Agricultural Research and General Legislation, and a copy of this testimony has been appended to my prepared statement.[18]

We especially support: equal attention to baking and other performance criteria for the U.S. market on a par with export quality considerations; national standards for release of new wheat varieties after extensive testing to ensure good baking quality; identification of performance characteristics of seeds by various means; periodic national surveys to determine the distribution of grain and oilseed varieties grown on farms; and consideration of a new "undesirable varieties" provision in the farm bill to help screen out those wheat varieties that are damaging the reputation of U.S. exports and destabilizing the quality of domestic wheat supplies.

Five, other issues.

ABA continues to support Federal preemption of State laws and regulations regarding pesticide residue tolerances in foods. Research investments on pesticides and other chemical tolerances in food should be greatly increased to study the effects of pesticides and other chemical tolerances in food, pursuant to many congressional and administration initiatives.

Mr. Chairman, thank you for the opportunity and I would be happy to respond to questions.

[The prepared statement of Mr. Marten and attached February 22, 1990, statement follow:]

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[18] Preparation for the 1990 Farm Bill, Enhancing Grain Quality (S. Hrg. 101-259, Part III), February 22, 1990, see pages 218-229 and pages 298-313. See p. 320 of this hearing.

AMERICAN BAKERS ASSOCIATION

Statement by Mr. Randy Marten, Representing the American Bakers Association before the Sub-Committee on Agricultural Production and Stabilization of the Senate Committee on Agriculture and Forestry

March 8, 1990

My name is Randy Marten. I am Vice President for Materials Acquisition and Transportation for Campbell Taggart Inc. I am here today on behalf of the American Bakers Association which represents companies that produce approximately 80% of the baked goods in the United States. We appreciate the opportunity to present the wholesale baking industry's views before this Committee today. The following issues are the most important to our industry.

1. Adequate supplies of wheat and other commodities for American consumers and export;
2. Price and income supports for farmers, to help insure a profitable and competitive agriculture;
3. Responsible operation of our export programs;
4. Grain quality improvements for domestic and export markets;
5. Human health, food safety, and the environment.

We wish to reaffirm our strong views on the need to reduce government intervention in agriculture and to let farmers produce abundantly for markets at home and abroad. At the same time, we recognize that farmers generally favor continuation of programs that support farm income. Maintenance of grain reserves and assurance of food safety also require a governmental role. Changes in the law are needed to give farmers more flexibility in operating their farms. The government should improve grain quality standards, and respond when exports face unfair competition. There is room for less government in agriculture, however, while carrying on the necessary activities cited above. Our positions in five key farm program areas are as follows.

1. Adequate Supplies of Wheat and Other Products

We believe that the acreage reduction program for wheat should be phased out over time. If retained, the program should be operated to maintain total wheat carryover at or near 40 percent of a year's needs for all purposes, including exports. That translates into carryover stocks of nearly 1 billion bushels of wheat on June 1 of each year. When stocks fall below that level, steps should be taken to increase them. If stocks are expected to be 25 percent of a year's requirements, farmers should be encouraged to produce wheat on all their available land. USDA may occasionally need to reduce wheat acreage if stocks are too large, but should never cut acreage by more than 20 percent.

Farm programs should provide more flexibility for farmers to determine their cropping patterns on the basis of market signals. Shortages of oats and oilseeds can be avoided if the programs for wheat, corn, and cotton would permit producers to respond to market signals while retaining their base acreages for program crops.

Consideration should be given to combining the farmer-owned reserve (FOR) and the food security wheat reserve, to minimize CCC ownership of grains. Shorter reserve contracts and lower release prices along the lines proposed by the Administration may serve as a pattern for amending present law.

No wheat land should be added to the Conservation Reserve (CR) after 1989. The 11 million acres of wheat land contracted by the end of 1990 have significantly reduced our capacity to produce. Any greater acreage in the CR could threaten both domestic and export supplies of wheat. We strongly urge the Secretary of Agriculture and Congress to delay any additional CR signup until after new criteria have been considered in the farm bill debate, possibly shifting the objectives of the CR from soil erosion to environmental improvement.

2. Price and Income Supports

We believe that the present formula for adjusting loan rates from year to year based on average market prices in three of the previous five years is workable for the 1990's. Increases as well as decreases in loan rates should not exceed 5 percent per year, however. This will help insure stable and competitive prices.

Target prices and deficiency payments have been of great benefit to farmers. They should be continued, and set from year to year consistent with farm income objectives, budgetary considerations, and any agreements made in the Uruguay Round to reduce world-wide agricultural protection.

3. Export Programs

We support U.S. policies to ensure a strong competitive position in world trade. The Export Enhancement Program (EEP) may need to be used in certain circumstances to meet competition from the European Community and other countries. However, it should be operated with greater consistency and openness than in past years, so that everyone affected may know what to expect. Revised rules in USDA, and proposals by

Congressman Glickman of Kansas go a long way toward achieving these objectives. Business-like use of export credit programs, and generous food aid programs also have our support.

The overall supply-demand balance for wheat, and the effect of EEP on U.S. food industries and the federal budget should influence the operation of our export assistance programs. It is appropriate to limit use of the EEP when stocks are low, as in 1989 and 1990. It may be equally appropriate to respond to aggressive use of export subsidies by other countries, if world wheat supplies again become excessive.

4. Grain Quality

The 1990 farm bill should make development and production of high quality wheats that meet the needs of bakers and consumers in the U.S. and around the world a top priority. We strongly support increased funding for USDA and University research on grain quality, but that is not enough. Specific proposals on grain quality were provided in testimony on February 22, 1990 before the Senate Sub-Committee on Agricultural Research and General Legislation (a copy is appended for your consideration). We especially support:

- Equal attention to baking and other performance criteria for the U.S. market on a par with export quality considerations;

- National standards for release of new wheat varieties after extensive testing to insure good baking quality;

- Identification of performance characteristics of seeds by various means;

- Periodic national surveys to determine the distribution of grain and oilseed varieties grown on farms; and

- Consideration of a new "undesirable varieties" provision in the farm bill to help screen out those wheat varieties which are damaging the reputation of U.S. exports and destabilizing the quality of domestic wheat supplies.

5. Other Issues

ABA continues to support federal preemption of state laws and regulations regarding pesticide residue tolerances in foods. Research investments on pesticides and other chemical tolerances in food should be greatly increased, pursuant to many Congressional and Administration initiatives.

The U.S. dairy program needs to be amended, to align our domestic policies with our international commitments, while assuring a stable supply of dairy products.

We urge that obsolete wheat certificate provisions left over from the 1960's be removed from the law. They are out of date, are not expected to be used again, and serve only to add confusion to the farm policy debate.

Mr. Chairman: I would be pleased to respond to questions.

AMERICAN BAKERS ASSOCIATION

Statement by Mr. Randy Marten, Representing the American Bakers Association before the Sub-Committee on Agricultural Research and General Legislation of the Senate Committee on Agriculture and Forestry

February 22, 1990

My name is Randy Marten. I am Vice President for Materials Acquisition and Transportation for Campbell Taggart Inc. I am here today on behalf of The American Bakers Association, the Biscuit and Cracker Manufacturers Association, and the Retail Bakers of America. Together, our associations represent companies that produce approximately 80 percent of all U.S. bakery products. The U.S. baking industry transforms more than 300 million hundredweight of flour, from nearly 700 million bushels of wheat into a wide variety of bakery products each year.

We commend Senator Daschle, Senator Bond, and others for introducing the Grain Quality Incentives Act of 1989. Most sections of the bill are directed toward the improvement of grain quality and cleanliness in order to compete more vigorously in world markets. We support that objective. We wish to call the Committee's attention to the fact that for wheat, quality requirements in respect to the eventual end-uses of the grain are increasingly similar for export and domestic markets. Physical soundness and purity are important criteria for wheat quality. But it is the intrinsic characteristics of wheat to efficiently and consistently produce the baked products desired by consumers that is crucial. We believe that is true for other grains, and for oilseeds as well.

Our concern about the baking performance of new wheat varieties is heightened by recent developments in plant breeding technology. A few wheat varieties brought from Russia and Turkey dominated U.S. hard winter wheat production from the late 19th century to about 1940. Since then, dozens of new

SUITE [illegible] • [illegible] N.W. • [illegible] D.C. [illegible]

varieties have been developed, released, improved, and then superseded in the past 50 years. Of the five leading hard winter wheat varieties in Kansas in 1980 none remained as a leading variety in 1989. This rapid turnover, with only limited end use testing of the new varieties being released, represents a cost to the domestic market and a risk to our export markets. It is of concern not only to bread makers, but to cookie and cracker manufacturers as well. For them, protein quality and excessive kernel hardness are the major issues.

The quality of wheat declined steadily during the 1970's and 1980's concurrent with the proliferation of varieties. Controlled laboratory bake tests for bread indicate that only 50 percent of flour samples tested in 1987 fell in the upper half of possible performance scores, against 96 percent in 1975. This is shown in detail in an Annex to my testimony which we wish to submit for the record. The industry feels that economic incentives need to be available to plant breeders and wheat producers to encourage production of better quality wheat in the interest of both exports and U.S. consumers of bakery products.

Our recommendations in respect to the bill are as follows:

1. Quality considerations for domestic use should be given equal billing with export requirements throughout the bill. The studies called for in Sec. 102 and 104 should deal explicitly with quality considerations for baking and other domestic uses as well as with the export factors cited in the bill. The Department of Agriculture should conduct these studies in association with representatives of State Agricultural Experiment Stations, farm groups,

grain exporters, the cereal foods industries, and the Office of Technology Assessment.

2. End-use evaluation of new wheat varieties for domestic and export use should be given a high priority in research conducted by the USDA and the State Experiment Stations. The federal Wheat Quality Laboratories in Kansas, Ohio, North Dakota, and the state of Washington need increased support and direction in this regard. These labs, properly staffed and equipped, have the potential to lead the way in the development of wheat varieties combining the needed attributes of yield, disease resistance, and performance or end use. Also, these labs could be in the forefront of developing improved flour quality tests for different baking needs to facilitate the screening of new varieties.

   These issues should be addressed more directly in the bill. We recommend that Sec. 601 be amended to include the certification of new wheat cultivars, and establishment of national criteria or quidelines for the release of new varieties of wheat by public and private plant breeders. We believe this consideration may apply also to other grains and to oilseeds.

3. We support the identification of performance characteristics of seed, by varieties, in the manner suggested in Sec. 701. These may need to be quite general, since environmental as well as genetic factors influence end-use

quality. This would serve as a guideline for farmers in selecting seed varieties, and as a general educational device for all elements of the industry. Sec. 702, however, relating to identifying varieties on warehouse receipts, may not be feasible.

4. We strongly support Sec. 703, providing for periodic compilation of the distribution and relative importance of grain varieties nationally. This report should also summarize the relevant quality characteristics of leading and emerging varieties, including end-use properties. This would aid in performance labelling of varieties, as provided in Sec. 701.

5. We support the idea of offering incentives through the price support system for clean and high quality grain. We note, however, that this has been studied by USDA and applied in various ways for many years with little success. We call the Committee's attention to an effective procedure that was once used for wheat -- the "Undesirable Varieties" list. When the price support loan was the key factor supporting prices, wheats placed on this list by USDA were usually withdrawn from production within a few years. Consideration should be given to the development of a new procedure, adapted to the fact that deficiency payments rather then price support loans now provide the most important financial incentives to farmers.

6. The language in Sec. 301 which would authorize the Secretary to prohibit or limit blending of grains could present difficult problems for the grain industry. There may be some merchandizing abuses relating primarily to grain for export that merit Congressional action, however. Provisions in Titles IX to XIII relating to grain quality in the Farmer-Owned Reserve, CCC, EEP, Crop Insurance and Disaster Relief Programs may be helpful, but general improvements in U.S. grain quality will help those programs as well.

Finally, the baking industry recognizes its responsibility to define its needs clearly, and to communicate those needs to growers, seed breeders, and millers. We look forward to working with Congress to enact key portions of this bill in 1990, and to working with all interested parties in a cooperative environment to improve grain quality across the board.

Senator **Boren**. Well, price stability obviously is very important to you in the decisions that are made in the industry, avoiding these wide price swings.

Mr. **Marten**. Well, we are all business people and we realize that there is an inherent risk in doing business. But as the gentleman, a farmer, said, there are risks involved in dealing in this business, be it the weather, be it in export demand, and to consider that the Government should be a partner in the process and not an enemy, and oftentimes the use and administration of export enhancement has been in such a way that it has created a lot more unpredictability than really should have been the case, in our opinion.

Senator **Boren**. Thank you very much.

Mr. Goulding.

STATEMENT OF STEPHEN H. GOULDING, PRESIDENT, OAK STATE PRODUCTS, INC., WENONA, IL; TESTIFYING ON BEHALF OF THE BISCUIT AND CRACKER MANUFACTURERS' ASSOCIATION (B&CMA), WASHINGTON, DC

Mr. **Goulding**. Thank you.

INTRODUCTION

I am Steve Goulding, president of Oak State Products, Inc., manufacturer of Archway Cookies, located in Wenona, Illinois, and surrounded by corn and beans.

Today I am speaking on behalf of the Biscuit and Cracker group and have with me Pat Mitchell, who is director of commodity purchasing for the Keebler Company. We represent about 85 percent of the cookie and cracker bakers in the United States. We have been encouraged by the direction of the agricultural policy as a result of the Food Security Act of 1985 (FSA), and what we had perceived as a strengthening of the farm economy, at least in the last 2 to 3 years in particular. But we particularly appreciate the concept of market orientation that has come into the FSA and look forward to the continued market orientation of the 1990 Farm Act.

FOUR SPECIFIC ISSUES THAT WE BELIEVE SHOULD BE ADDRESSED AS AGRICULTURAL POLICY IS REVIEWED

Today we would like to focus on four specific issues, not addressing the dollars involved or the budget considerations, which we feel are better left to other groups.

PLANTING FLEXIBILITY

The first is the planting flexibility. We support an increase in planting flexibility, but one that is not linked to budget savings. The current rigidity of several sections of the agricultural policy, we believe, will inhibit the full participation in expected consumption increases, both at home and in the world market, in the years to come.

ACREAGE PRODUCTION PROGRAMS

Second, in the acreage reduction programs, we want to point out that the CRP has already reduced 34 million acres and the legitimate question would be do we need ARP's for anything other than budgetary purposes? We would support a mechanism similar to Secretary Yeutter's February 6 proposal.

FARMER-OWNED RESERVE (FOR)

Third, in the farmer-owned reserve, we believe the FOR should exist as a buffer stock mechanism in the truest sense, rather than a price support mechanism with release levels well above loan rates. We support a program similar to that proposed by the Secretary, but would look for release levels at prices closer to the loan rates.

EXPORT ENHANCEMENT PROGRAM

Fourth, in the Export Enhancement Program, we will continue to support the EEP for bulk commodities. We believe that the U.S. farmers' competitiveness in the world arena should not be inhibited by the unfair trade practices of others.

The 1985 FSA had as its fundamental purpose, the need to return to a more market oriented agricultural policy. The B&CMA supports the basic policy direction set forth in this act. Our suggestions are an attempt at adapting the FSA to the environment we foresee in the future. We believe it is imperative that as the focus of agricultural policy shifts to the 1990's, this policy direction is maintained and enhanced.

I would like to thank the subcommittee for the opportunity for the Biscuit and Cracker Manufacturers' Association to testify today and we look forward to working on the development of the farm bill.

[The prepared statement and 1990 Farm Bill Position Paper of Mr. Goulding follow:]

Statement of the Biscuit and Cracker Manufacturers' Association before the Subcommittee on Agricultural Production and Stabilization of Prices of the Senate Committee on Agriculture and Forestry.

March 8, 1990

The Biscuit and Cracker Manufacturers' Association
1400 L Street NW Suite 400
Washington, D.C. 20005

Good Afternoon.

My name is Stephen H. Goulding. I am President of Oak State Products, Inc., a baker of Archway Cookies. Our bakery is located in Wenona, Illinois. I am here today on behalf of the Biscuit and Cracker Manufacturers' Association (B&CMA). Accompanying me are Francis P. Rooney, President of the B&CMA and Patrick D. Mitchell, Director of Commodity Purchasing for the Keebler Company.

The Biscuit and Cracker Manufacturers' Association is the national trade association for the cookie and cracker industry. Our members manufacture 85 percent of all cookies and crackers baked in the United States.

The membership of the B&CMA has been encouraged by the direction of U.S. agricultural policy as a result of the 1985 Food Security Act (FSA). A strengthened farm economy is the success we immediately relate to the FSA, but it is the concept of market orientation that in the long run may be its most visible achievement. We support the market oriented course initiated in the 1985 FSA, and look for continued progress down this path as the 1990 Farm Bill is written.

The position paper we present today focuses on four (4) specific issues that we believe should be addressed as agricultural policy is reviewed:

Planting Flexibility: We support a plan which increases planting flexibility; however, one that does not link itself to budget savings. The current rigidity of several sections of agricultural policy will inhibit full participation in expected consumption increases in the world, including domestic, in the years to come.

Acreage Production Programs: We first bring to surface the amount of acreage already placed or planned to be placed in the Conservation Reserve Program (CRP). With 40-45 million acres of land idled through the CRP, a legitimate question could be ... why do we need ARP's for other than budgetary purposes? We support flexible ARP's, and would support a mechanism similar to that in Secretary Yeutter's February 6th proposal.

Farmer Owned Reserve:	We believe that the FOR should exist as a buffer stock mechanism in the truest sense, rather than a price support mechanism with release levels well above loan rates. We support a program similar to that proposed by the Secretary, but would look for release levels at prices significantly closer to loan rates.
Export Enhancement Program:	The B&CMA has and will continue to support the use of EEP for bulk commodities. We believe that the U.S. farmers' competitiveness in the world arena should not be inhibited by the unfair trade practices of others.

The 1985 FSA had as its fundamental purpose, the need to return to a more market oriented agricultural policy. The B&CMA supports the basic policy direction set forth in this Act. Our suggestions are an attempt at adapting the FSA to the environment we foresee in the future. We believe it is imperative that as the focus of agricultural policy shifts to the 1990's, this policy direction is maintained and enhanced.

I would like to thank the Committee for permitting the B&CMA to testify today, and we look forward to working with you in developing the 1990 Farm Bill.

1990 FARM BILL POSITION PAPER

The Biscuit and Cracker Manufacturers' Association
1400 L Street, N.W., Suite 400
Washington, D. C. 20005

The 1985 Food Security Act (FSA) was drafted during a period of excessive government stock levels, and eroding producer incomes. In response, the FSA focused on market orientation, primarily through reducing U.S. price supports in an effort to rebuild export competitiveness. The Act has succeeded in moving agriculture in the right direction by strengthening the farm economy. Despite this move towards more market orientation, U.S. farm programs still contain many rigid and inflexible provisions. Our purpose in this paper is to identify, review and suggest some alternatives to these inflexible and rigid provisions, which have actually led to increased government involvement in several agriculture sectors. We believe our proposals are the next step in an ongoing process to inject flexibility and market orientation into U.S. agricultural policy.

As we enter the final decade of the 20th century, expectations are for continued increases in world consumption of most agricultural products, food and feed grains, and oilseeds in particular. The acreage and supply control programs currently residing in farm legislation, along with the inflexibility that they personify, are not sufficient to allow the United States to participate in the expected growth outside its borders, and at the same time, fulfill the growing needs at home. Within this framework, we believe the issues of Planting Flexibility, Acreage Reduction Programs, Farmer Owned Reserves and the Export Enhancement Programs deserve to be addressed.

Planting Flexibility

During a joint hearing of the House Agriculture Subcommittees, USDA Deputy Undersecretary John Campbell stated that "in the simplest terms, the USDA wants producers to make their cropping decisions in response to market forces." Mr. Campbell stated that planting flexibility is the desired goal. Outlining guidelines for possible flexibility provisions to be included in the next farm bill, Mr. Campbell cautioned on the potential for increased costs associated with flexibility, including larger government expenditures, an inability to impact short-term demand, and lower income to producers. Specifically:

- Increased flexibility should mean greater latitude to respond to market signals, not subsidy benefits. Producers should not be given greater incentives to "farm the programs".

- If subsidies are linked to plantings, and plantings are freed up, planting flexibility should be accompanied by a realignment of target prices. The target price benefit is not equivalent across commodities relative to the cost of production. Producers will base their cropping decisions on target prices rather than market return.

- Planting flexibility should address the soybean issue, the uncompetitiveness of soybeans to program crops in most areas.
- Planting flexibility must not bust the budget, must be equitable to both program and non-program crop producers, and must be limited to those producers who plant or would have planted if not for the increased planting flexibility.
- Increased flexibility should not jeopardize conservation provisions of the 1985 FSA.

We would agree with these guidelines set forth by the USDA, except for the final point on conservation efforts. While we agree with the conservation intentions of the FSA with respect to wheat, the program has become a flexibility inhibitor. From its inception, through the seventh sign-up, the Conservation Reserve Program (CRP) has retired 14% of this country's wheat base acres. As the results from the most recent sign-ups are made public, it is likely that additional wheat acres will be removed from production, further limiting the amount of wheat base acreage (assuming a zero ARP) available to meet growing world and domestic needs into the 1990's.

Providing farmers with increased flexibility is an issue which is currently being debated within the agriculture industry. Planting flexibility has garnered renewed interest, as U.S. planted acreage of several crops, including oilseeds and oats, has shifted to foreign resources, primarily due to several inherent inflexibilities in the 1985 FSA. As a case in point, over the past 10 years, the U.S. has lost 11.7 million soybean acres, while South America has enjoyed a 15.7 million acre increase.

Following the guidelines set out by the USDA, we support a plan which increases planting flexibility; however, one that does not link itself to budget savings. Some have suggested that this could be resolved by basing deficiency payments, as they are now, on the base acreage, less set-aside. Thus, even the "freed up" acres would still be eligible for a deficiency payment of the base crop. This would allow the producer to make planting decisions based on market signals without loss of income support protection. To address the increased supply concerns of non-program farmers, limitations on acreage for specific, non-program crops, could be enacted.

Export Enhancement Program

The B&CMA has supported the used of the Export Enhancement Program (EEP) for bulk commodities since its inception in 1986 as a tool to fight the use of unfair trade practices. However, the B&CMA has and will continue to oppose the use of EEP for value-added products, such as wheat flour and vegetable oil, and in situations where domestic supplies are at risk.

Our support for the EEP has been based on what was perceived as the original objective of the program -- to regain market share which had been lost due to unfair competitive practices. We do not support the position that continuous subsidized U.S. sales of agricultural products is necessary to remain a viable supplier in the world market.

The B&CMA continues to support the use of the program for bulk commodities to meet this important objective. However, over the last two years the EEP has changed its focus from counteracting the use of unfair trade practices to becoming a mechanism to relieve the USDA's Commodity Credit Corporation of surplus stocks. In the 1985/86 marketing year, 15 percent of U.S. wheat exports were under this program, while during the 1987/88 and 1988/89 marketing years EEP accounted for 61 and 55 percent of U.S. wheat exports respectively. The growth in the use of the EEP for purposes beyond its original scope has created a situation where domestic users of U.S. wheat have been forced to pay a higher price than many importing countries.

Recently the USDA revised the EEP guidelines ostensibly to tighten the program's scope. We applaud the Administration for what we perceive as an attempt to redirect the program back to its original intent. However, the guidelines deviate from this objective when they state "targeted countries are those where U.S. sales have been non-existent..." and "all EEP initiatives must demonstrate their potential to develop markets for U.S. agricultural commodities..." These statements seem to undermine the original intent of the program, as they could legitimize subsidized exports to all importers.

The membership of the B&CMA supports a continuation of the Export Enhancement Program for bulk commodities, but only under the proposed original objectives of re-capturing market share lost to unfair competitive practices.

Acreage Reduction Program

Supply management policies have been a part of U.S. agriculture for more than 50 years; beginning with mandatory controls, but have evolved over time into a voluntary approach, which uses program incentives to entice farmers into idling productive acreage. The 1985 FSA utilizes two production control programs to manage surplus agriculture supplies; the Acreage Reduction Program (ARP), and the Conservation Reserve Program (CRP).

At the heart of the Acreage Reduction Program is the base acreage concept, which limits production that is eligible for program benefits. In the past, those benefits have proved attractive enough to entice farmers into maintaining and/or exceeding their base acreage by planting the maximum allowed each year. This reality occurs in spite of the commodities' respective supply/demand and price situations. Reliance on this historical base concept reduces producers' planting flexibility, distorts production patterns, and in the end, inhibits their ability to react to market signals.

Production controls, in combination with price supports have lifted commodity prices, and improved some farmers' income; however, past experience demonstrates that the effects are relatively short lived, and have proven counterproductive over time. One of the main problems with most forms of production controls is that prolonged use reduces their effectiveness. As the U.S. limits outputs and increases prices, the rest of the world adjusts to this artificial scarcity by expanding their domestic production. The twofold result of U.S. production controls is to lose export markets and to limit the farmers' incentives to remain competitive.

An unexpected fear of base expansion and/or base "creep" has resulted in an ARP rigidity, which has kept ARP's in place even though the supply/demand fundamentals of the respective commodity may not warrant any acreage set-aside.

The B&CMA believes that a zero percent ARP should be a viable program option. A case in point is wheat, where the Conservation Reserve Program has materially reduced its base acreage to the level where acreage set-aside is no longer necessary to control output. Through the sign-ups to date, a skewing of base acreage retirement can be seen for one crop (i.e. wheat) versus the other commodities. Under this 10 year land retirement scheme, there is limited opportunity to bring this base acreage back into production, regardless of the supply/demand and price signals. Consider the fact that the USDA felt the crop's supply/demand fundamentals justified (for the 1990/91 crop year) allowing producers to plant 105% of their base acres.

Farmer Owned Reserve

The Farmer Owned Reserve (FOR) was established in the 1977 Food and Agriculture Act, and amended in the 1985 Food Security Act, to provide storage for wheat and feedgrains when they "... are in abundant supply, and to extend the time period for their orderly marketing." Furthermore, the Reserve has established safeguards to assure that wheat and feed grains held under the program "...shall not be utilized in any manner to unduly depress, manipulate, or curtail the free market ... and provide for adequate, but not excessive, carryover stocks to ensure a reliable supply of the commodities."

In the early 1980's, the FOR drifted away from its stated purpose to usurp the role of a price support tool by isolating large quantities of grain from the market. These stocks can become "trapped" in the FOR because of its release prices, which are both too high and too inflexible to be responsive to market demand. As a case in point, there currently exists a situation where wheat is being drawn out of the Emergency Food Reserve, by Presidential decree, to meet food aid needs, while comparable stocks remain unavailable in the FOR.

The mechanisms governing the release of FOR stocks have caused marketing incentives to be overwhelmed by storage incentives, even in the face of strong prices. In addition, the FOR has at times been plagued by frequent program changes, as it has become a political tool, experiencing abrupt rule changes to serve short-term government objectives.

As in the case of EEP, the B&CMA believes the FOR should be redirected back to its original objective: to encourage orderly marketing, provide a buffer stock for weather and economic shocks, and ensure a reliable supply of U.S. grains.

The release of grain from the Reserve is set by law at 140% of the loan rate, or the current target price, whichever is higher. This artificially high release price, causes domestic users and importers to turn to cheaper alternatives, resulting in lost demand and large stocks being locked in the Reserve. We suggest that storage payments to the farmer cease, when the market price exceeds 140% of loan rates, allowing farmers to market their Reserve grain.

Currently, producers receive storage payments for their FOR grain one year in advance. If producers should wish to market their grain, any unearned storage payments must be repaid. The psychological factor of repaying unearned storage as well as the cash-flow aspect provide a barrier to selling, when compared to the market price received. To remove this built-in disincentive, we suggest that future storage payments be made on a quarterly basis.

Lastly, we recognize the need to maintain a food security reserve, and to meet humanitarian needs. However, it is important to note that the FOR was not created to be the primary vehicle for fulfilling emergency needs. The FOR is part of a larger strategic reserve that also includes a 147 million bushel Emergency Food Security Reserve and a 75 million bushel Disaster Reserve for feed grains.

Conclusion

The 1985 Food Security Act, had as its fundamental purpose, the need to return to a more market oriented agricultural policy. The B&CMA supports the basic policy direction set forth in this Act.

Although, as we have in the past, we will continue to make recommendations to adapt the 1985 farm legislation to the environment of the 1990's. We believe it is imperative that the new Bill maintain and enhance this policy direction.

Senator BOREN. Thank you very much. We appreciate your testimony.

Mr. Lyons.

STATEMENT OF DAVID LYONS, MEMBER, BOARD OF DIRECTORS, NORTH AMERICAN EXPORT GRAIN ASSOCIATION (NAEGA), WASHINGTON, DC

Mr. LYONS. Thank you, Senator.

INTRODUCTION

I work for the Louis Dreyfus Corporation here in Washington and I am here representing NAEGA.

DOMESTIC POLICY IS KEY

Domestic farm policy is the foundation for the competitiveness of U.S. agricultural exports. You know, you can do all the export programs in the world you want to, but you have to start with the right domestic policy.

One only has to look back to the early 1980's to see some of the problems we had there where you had loan rates that were too high, priced you out of world markets, and then we stored, through our stocks policies, we didn't market, we stored, let other people produce and market. And then as outlays got big, then we had massive acreage reduction programs.

1985 FARM ACT A MAJOR IMPROVEMENT

The 1985 farm bill changed a lot of that, but there are still some things to do, and at least three things come to mind.

ACREAGE REDUCTION PROGRAMS

The 1990 farm bill must build on this success. I think number one is probably acreage reduction programs. When you think about it, you know, these ARP's are kind of a throwback or remnant to the old supply control types of policies. They are still around really basically for budget reasons. You know, as you look to the future and you want to be competitive, why do we have ARP's? Really only for budget reasons, and I think we ought to try to eliminate those things. It is an inefficiency, a drag. You know, farmers have to spread their fixed costs over fewer acres. I think it is a bad thing.

LOAN RATES

One of the great achievements of the 1985 farm bill was that we got loan rates down. A formula concept for loan rates was instituted with a further Findley reduction. We ought to retain that. It is ironic that people are talking about changing loan rates after the success of the 1985 farm bill. Some are talking about a slight increase in loan rates, that sort of thing, just at the time when I think the formula is really going to start to work. You might have a little bump up in loan rates from the formula, but any kind of an effort to arbitrarily increase loan rates would be a big mistake.

Really, it would mean that we failed to learn the lessons of the early 1980's.

Senator **Boren**. Is using the Findley—you heard our discussion earlier in which I was asking about the Findley. I mean, I agree with you in what you are saying, but do you think it made us more competitive to drop that on down with the Findley under those circumstances, even though you already had an 80 cent gap on price already between loan rate and market price?

Mr. **Lyons**. I think the Findley, the further 20 percent adjustment, really was very important, and I think that should be retained. I think you are right at the point though where loan rates are not going to continue to rapidly escalate downward. In fact, with the high prices of last year caused by the drought of 1988, I think you might get a situation where you might have loan rates level off, or you might even have a slight bump up in the loan rate. But it should be market driven. That is the point. And that will get you to market clearing loan rates in most years, especially when you set it at 75, 85 percent, whatever of the 5-year average market price.

PLANTING FLEXIBILITY

The third thing is planting flexibility. You need to have market driven planting flexibility, not simple base substitution. Which is target price driven planting flexibility, where the acreages will shift to the most lucrative benefits under the farm program. That would be a mistake. In a sense, that would make things worse than you have now. You know, if we think that acreages are shifting to corn because of high deficiency payments now, base substitutions would exacerbate the situation. So those are the three things.

GRAIN RESERVE STOCKS POLICIES

The stocks policy is very, very important, and it is the one thing that was not changed in the 1985 farm bill. Nobody thought about it. Stocks were so big nobody ever thought we would get to the point where you had to do something about it. Very, very important. The real problem with it is that the release levels are too high. What happens is you get a drought like you had in 1983, prices rally, demand is choked off, foreign producers start producing before you get a chance to get those bushels back in the market. Certificates are what allowed the 1985 farm bill to really work, and now that will be foreclosed because we don't have stocks. So that is very, very important.

GSM GUARANTEED EXPORT CREDIT

I see my time has run out. I need to say something about export credit guarantees, GSM credit guarantees. In many ways those are the most important tools that we have to build export markets and to meet the competitive situation with the Europeans.

Senator **Boren**. New opportunities as well.

Mr. **Lyons**. Yes, and we have changes in Eastern Europe. We may have a waiver of Jackson-Vanik for the Soviet Union. We need to have the maximum possible level of credit guarantees.

Senator **Boren**. Increase the legal level of authorizations from the current level.

Mr. **Lyons**. I think it needs to be clearly looked at.

Senator **Boren**. Five billion, I believe, and some of us have suggested going to seven.

Mr. **Lyons**. Right, and I think that needs to be very strongly looked at. We could say something about EEP, but I think there was a hearing a couple weeks ago and Bill Allen of Union Equity I think was here. NAEGA has some proposals on the Export Enhancement Program. I think I would just leave it at that.

[The prepared statement and the attached paper, "The Export Enhancement Program (EEP): A Proposal for Change" of Mr. Lyons follow:]

North American Export Grain
Association Incorporated

Statement of

DAVID LYONS
Director
NORTH AMERICAN EXPORT GRAIN ASSOCIATION

At Hearings on Wheat Program Issues
SUBCOMMITTEE ON AGRICULTURE PRODUCTION AND STABILIZATION OF PRICES
U.S. SENATE
March 8, 1990

It is a privilege to join you today. I am David Lyons, Vice President, Louis Dreyfus Corporation. I appear before you today in my capacity as a member of the Board of Directors of the North American Export Grain Association (NAEGA), the national association of U.S. grain and oilseeds exporting companies and cooperatives. I am accompanied by Steve McCoy, President of NAEGA.

NAEGA member companies originate perhaps 90% of all U.S. wheat exported to destinations throughout the world. We have a obvious interest in all government policy affecting U.S. wheat production and marketing. We are pleased by the opportunity to testify today. We look forward to working together with you to formulate policy dedicated to the maintenance of U.S. competitiveness and a healthy and profitable U.S. agricultural economy.

DOMESTIC POLICY IS KEY

Domestic farm policy is the foundation for the competitiveness of U.S. agricultural exports. Competitiveness is the key to growth in agricultural exports; and agricultural exports are the key to a stable prosperous U.S. agriculture.

One only has to look back to the early 1980's to see how ill-advised farm policies can contribute to lost export markets, growing stocks, lower farm prices, huge government farm program costs, lower farm income, and financial distress for U.S. agriculture. Escalating loan rates in the early 1980's helped price U.S. products out of world markets. At these loan rates, the U.S. government, and not the world market, became the buyer for U.S. commodities.

The government then stored these commodities either in CCC inventory or through the Farmer Owned Reserve (FOR). This allowed competitors to produce for world market needs, while the U.S. stored huge stocks. Finally, as stocks grew ever larger, farm program cost pressures forced the Department of Agriculture (USDA) to implement huge acreage idling programs. This only further

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allowed competitors to produce for export markets the U.S. was abandoning.

1985 FARM ACT A MAJOR IMPROVEMENT

The market oriented policies of the 1985 farm bill have led to a major improvement in the conditions facing U.S. agriculture. They have contributed to a dramatic turn-around. Exports and domestic use have increased. Stocks have been reduced. Farm income has been at record levels for the last three years. Farm program costs have been cut in half. Land values have stabilized, or increased in many areas. Agricultural debt has been reduced. The financial position for most farmers has improved and they feel better about their future than in 1985.

The 1990 farm bill must build on this success. For U.S. agriculture to reap the rewards of growing world markets in the 1990's, the market oriented policy direction of the 1985 farm bill must continue in the 1990 farm bill. However, some improvements in the 1985 farm bill must be made so U.S. agriculture can respond to world market opportunities.

ACREAGE REDUCTION PROGRAMS

Annual acreage reduction programs (ARPs) should be eliminated in the 1990 bill. Not only do ARPs increase production costs and reduce the efficiency of U.S. agriculture, they encourage foreign production that will compete with U.S. production in world markets.

Annual acreage reduction programs are a tool of an outdated "supply control" orientation in farm policy; they are not an appropriate tool to meet world market demand in the 1990's.
As a practical matter, the Congress needs to remember that with one year left, the Conservation Reserve Program (CRP) has already removed from production 34 million acres, of which over 20 million acres have been farm program crop acreage base. The crop acreage bases already removed from production by CRP constitute in effect about a 10 percent ARP over all crop acreage bases. The CRP has been a big success in meeting conservation goals and removing very marginal land from production. With this amount of aid already in CRP, the Congress must seriously question the desirability of further annual ARPs.

LOAN RATES

Market driven loan rates must be continued in the 1990 farm bill. The concept of determining loan rates based on a percentage of an average of previous year market prices is a good one. It should result in market clearing loan rates. The Congress must avoid the temptation to increase loan rates. To arbitrarily increase loan rates would repeat the mistakes which contributed to the difficulties of the early 1980's.

PLANTING FLEXIBILITY

The Congress must provide flexibility for farmers to make production decisions based on market signals instead of farm program benefit signals. In the past, market prices for soybeans or for oats have been strong, but high target prices or the need to plant a given crop to maintain a crop acreage base have provided the incentive to plant for the farm commodity program rather than the market. The inflexibility of the commodity programs has contributed to a shifting of world soybean production from the U.S. to South America; and to increased importation of oats into the U.S.

Many different techniques for providing flexibility have been discussed and are possible; the important objective, however, is to provide flexibility which is market price driven. Target price driven flexibility would only provide for further distortion in farmer production decisions.

GRAIN RESERVE STOCKS POLICIES

Grain reserve stocks policies are an integral part of overall farm policy and are critical to the competitiveness of U.S. agriculture. Generic certificates were the market oriented stocks policy of the 1985 farm bill. Generic certificates allowed the Secretary of Agriculture to make government controlled stocks available to the market at realistic market prices. Since stock levels are now reduced, generic certificates will be much less available. This makes it doubly critical to make changes in grain reserve policies.

Stocks policies should be as simple as possible, provide flexibility to meet changing market conditions, and treat reserve stocks as a legitimate buffer, so that they are available when there is humanitarian and commercial need. Since reserve stocks should be only a buffer, the quantity in a reserve should not be large. Large stocks simply overhang the marketplace, depressing upward price movements. While stocks can be isolated from the market in the short term, forcing prices higher than they otherwise would be, the stocks always exist and at some time must return to the market. Reserves cannot take the lows out of a weak market without taking the highs out of a stronger one.

Reserves were first made a formal part of the United States farm programs in the early 1970's in response to concerns over the possibility of scarce food supplies. There were, of course, reserves before that time which were carried by the market. No government reserve is necessary to carry stocks through the year. Reserves can and will be carried by the market. The market functions to allocate supplies throughout the year by building in carrying charges which entice both farmers and merchants to carry stocks forward.

FOOD SECURITY WHEAT RESERVE

The Food Security Wheat Reserve (FSWR) is authorized at 147 million bushels of wheat to be used only for humanitarian purposes. The FSWR should be continued in the 1990 farm bill. The FSWR is limited in size; and the purpose for which the stocks can be used is specifically laid out. The FSWR provides assurance that U.S. food aid commitments can be met.

FARMER-OWNED RESERVE (FOR)

The Farmer-Owned Reserve was established in the 1977 Food and Agriculture Act to allow producers of wheat and feed grains to store such commodities when they "...are in abundant supply and extend the time period for their orderly marketing." The Act provides that "...the Secretary shall establish safeguards to assure that wheat and feed grains held under the program shall not be utilized in any manner to unduly depress, manipulate, or curtail the free market."

The 1985 farm bill added the following phase to the purpose: "...and provide for adequate, but not excessive, carryover stocks to ensure a reliable supply of the commodities." Despite the stated purpose of the reserve, reserve policy moved in a different direction following the 1980 grain embargo. The FOR took on the role of a price-support tool to isolate large quantities of grain from the market. With quantities locked away, free stocks became tight, pushing market prices up, and letting other exporters take business away at prices just below FOR release prices. The FOR, like ARPs, made the United States uncompetitive.

The purpose of the FOR should be clearly defined: it should be to encourage orderly marketing, provide a buffer stock for weather and economic shocks, and ensure a reliable supply of U.S. grains. Without a clear purpose, the reserve may again be asked to become a price support tool.

Since the FOR should be a buffer stock, not an entitlement program for storage payments to farmers, the size of the FOR should be kept to a level consistent with its use as a buffer stock. A clear maximum should be determined, perhaps 300 million bushels of wheat, 450 million bushels of feedgrains. Under current provisions, entry is largely at the discretion of the Secretary of Agriculture within the parameters set by law. Discretionary authority for the Secretary is appropriate and should be retained. But the Secretary should be precluded from allowing entry when prices are strong. This approach would be consistent with the purpose of the reserve. When prices are strong and the market is calling for those bushels, there is no reason to build stocks.

Currently, the release of grain from the reserve is set by law at 140 percent of the loan rate or the current target price, whichever is higher. Long before prices reach this high release level, domestic and export demand has been lost. In 1983 for example, this resulted in large stocks being locked in the FOR while domestic livestock producers were reducing livestock numbers and foreign buyers were looking for alternative sources of supply.

Release price levels need to be lower in order for the reserve to effectively function as a buffer stock. Once release level is reached, storage payments to farmers should cease. Market incentives for farmers to sell their crops should not be overwhelmed by storage incentives. Instead of making the full storage payment in advance, payments should be made only after storage has been earned.

The length of FOR contracts also needs review. Under current law, the FOR agreement extends the original loan for three years. This has proved to be too long of a time period. The FOR contract be limited to a maximum of 18 months beyond the 9 month price support loan term with no extensions permitted. This step would keep the reserve fluid, with grain moving through and not encourage a large reserve build-up. This change would also mean a lower likelihood of quality related deterioration.

COMMODITY CREDIT CORPORATION (CCC) INVENTORY

CCC Inventory is made up of stocks acquired through loan forfeitures. By law, these stocks cannot be sold on the market for a price less than 110 percent of any FOR trigger price. Only through certificates and auctions were these stocks made available to the market for the past four years.

The problem with CCC resale prices is the same as FOR release levels -- they are too high. To keep those CCC acquired stocks liquid, resale prices need to be set at lower levels.

GSM GUARANTEED EXPORT CREDIT

Maintenance of adequate government guaranteed GSM export credit is absolutely essential, if the U.S. is to continue to build new markets abroad, and meet competitive pressures arising from unfair foreign trade practices and the inability of some developing countries to finance purchases of U.S. wheat.

The GSM export credit program is our Nation's lifeline to some of our most important overseas customers. In this regard, export credit is more vital than any other program we currently offer such countries, including EEP.

GSM credits should be supported and funded at the maximum levels possible, consistent with their potential need in the future. That need increases as we consider new opportunities arising in Eastern European countries; and changed conditions in

U.S.-Soviet trade arising from waiver of the Jackson-Vanik amendment. Consideration should be given to management improvements in GSM credit programs designed to eliminate "red tape" and provide for their expanded use. Such changes in these programs could make them more attractive to exporters and foreign customers alike, providing new demand for U.S. wheat in future years.

EXPORT ENHANCEMENT PROGRAM

Pending changes in the export enhancement program (EEP) arising from the current inter-agency review, legislation should be considered to add greater stability and transparency to the EEP program.

The program currently operates in a manner prejudicial to U.S. farmers and grain exporters. Specific changes recommended by NAEGA include provisions requiring that the program allow:

(1) negotiation directly between buyer and seller, eliminating the government role in determining price, shipment period, coast of shipment, class and grade of grain, and other conditions of sale;

(2) contracting for any class or classes of grain for shipment from any coast or coasts;

(3) switching of classes and grades of grain and coasts of shipments at any time prior to shipment by agreement of contract parties;

(4) a single bonus to apply to all classes of wheat (other than durum) with an "additive bonus" if necessary to counter particularly aggressive foreign subsidization;

(5) public announcement of a list of EEP eligible countries or an annual "EEP marketing plan" designed to add transparency to the program; and

(6) elimination of certain "nuisance" and anti-competitive provisions of current regulations.

More detailed information regarding these matters is contained in the pages attached to this testimony. NAEGA welcomes your review and comments regarding the recommendations made.

CONCLUSION

In conclusion, the 1990 farm bill must maintain and improve on market oriented policies of the 1985 farm bill. Annual ARP's should be eliminated. Market determined loan rates must be continued. Producers must be given flexibility to produce based on market signals instead of farm program signals. Grain reserves, both FOR and CCC inventory, must be accessible to the market at lower price levels. Adequate GSM export credit must be available to finance wheat sales. Finally, the EEP should be maintained only for trade policy negotiating purposes. If maintained, EEP should be made a more flexible, stable and transparent tool of U.S. policy, along lines we have suggested in this testimony.

I thank you for this opportunity to testify today. Of course, we stand ready to assist you as we can in your important work on the 1990 farm bill. We look forward to future opportunities to discuss our specific recommendations in greater detail. I am happy to answer any questions that you may have.

NAEGA
North American Export Grain
Association Incorporated

THE EXPORT ENHANCEMENT PROGRAM (EEP): A PROPOSAL FOR CHANGE

Recommendations of the North American Export Grain Association

May 1989

Introduction

In testimony presented before the House Subcommittee on Wheat, Soybeans, and Feed Grains on April 27, 1989 (see attached), the North American Export Grain Association (NAEGA) has recommended "redesign" of the current export enhancement program (EEP) to "lessen the adverse impact of government in the grain marketing process".

The EEP currently "acts as a deterrent rather than as a stimulant to export sales", the testimony states: "foreign grain customers look to the U.S. government rather than to the marketplace to make basic decisions regarding purchases". The testimony notes that "a greater element of stability, consistency and predictability is necessary in the EEP program, if it is not place an unreasonable burden on grain markets". It also notes that "greater transparency in the decision-making process would result in improvement in the program".

The following information is provided as additional to the views expressed in NAEGA's April 27 testimony. The North American Export Grain Association (NAEGA) represents the interests of U.S. grain and oilseeds exporting companies and cooperatives.

The Current System

Currently, USDA -- either internally, or, more often in negotiation directly with a foreign buyer (usually a government) -- determines the terms of sale of commodities sold under the export enhancement program (EEP) down to specifics including shipment period; coast of shipment; class and grade of grain; and, in many cases, price. Once these initial determinations are made, the buyer invites exporters to bid for the business.

USDA calculates the bonus it believes is needed to buy-down the price of the commodity to the price offered by the EC for the commodity in the market in question. An exporter or exporters offering to sell within the bonus range may be granted a bonus and thereby the business.

However, the process is not automatic. Prices and acceptable bonus levels vary from day to day; and from period to period. USDA, by exercising total discretion with respect to such sales, may reject or accept on any given day business offered at terms better or worse than those offered on the previous day or day following.

There is an absence of consistency and predictability in the program.

The Current Problems

The negotiation of contract terms and the setting of bonus levels by USDA takes away from the exporter the ability to rearrange domestic positions to benefit from the most efficient and advantageous terms; and prevents competitively placed producers from participating in the sale to the extent that they would under free market conditions.

By tightly limiting the shipment, the present system prevents the buyer from making any substantial forward purchases. EEP initiatives are offered piecemeal. A buyer who may be disposed to buying substantial quantities of grains in predictable conditions is precluded from that option because he cannot predict when the next initiative will take place. The lack of consistency and predictability in the program creates frustration for both buyer and exporter, results in charges of buyer "discrimination" and, in the long term, will tend to drive our best volume customers to more predictable origins.

Indeed, this may already have happened. Producer, buyer and exporter all fail to benefit from the program as Congress intended. Significant sales and, hence, purchases from producers go unmade.

A Partial Solution

There is no perfect "market-oriented" solution to problems of this nature created by a targeted export subsidy program which, by its very nature, impedes the normal function of markets. Nevertheless, certain improvements in the current system could be made which would restore to a greater extent the operation of the free market to the benefit of the program and affected parties, including exporters and producers.

NAEGA has reviewed some possible solutions. Among these, we recommend the following:

(1) NEGOTIATIONS SHOULD BE DONE DIRECTLY BETWEEN BUYER AND SELLER, ELIMINATING THE GOVERNMENT ROLE IN DETERMINING PRICE, SHIPMENT PERIOD, COAST OF SHIPMENT, CLASS, AND GRADE OF GRAIN, AND OTHER CONDITIONS OF SALE.

(2) THESE NEGOTIATIONS SHOULD PERMIT THE CONTRACTING FOR: (a) ANY CLASS OR CLASSES OF GRAIN; AND (b) SHIPMENT FROM ANY COAST OR COASTS.

(3) CLASSES AND GRADES OF GRAIN AND COASTS OF SHIPMENT SHOULD, AS IN THE FREE MARKET, BE SWITCHABLE AT ANY TIME PRIOR TO SHIPMENT BY PRIOR AGREEMENT OF BUYER AND SELLER.

(4) THE SAME BONUS SHOULD APPLY TO ALL CLASSES OF WHEAT (OTHER THAN DURUM) FROM SHIPMENT FROM ALL COASTS.

IF NECESSARY, AN "ADDITIVE BONUS", SUCH AS THAT THE EC NOW EMPLOYS, COULD ALSO BE GRANTED AND, IF GRANTED, PUBLICALLY ANNOUNCED, TO COUNTER PARTICULARLY AGGRESSIVE SUBSIDIES APPLIED TO EXPORTS OF OTHER ORIGINS OF A GIVEN COUNTRY.

(5) TRANSPARENCY AND STABILITY SHOULD BE ADDED TO THE MARKET.

For example, USDA could, not later than the beginning of each crop year, announce an "EEP marketing plan" specifying eligible countries and quantities of commodities available for such countries under the program.

If, under this type of scheme, the quantities specified for any individual country had not been contracted for within six months of the announcement of the plan, the quantities specified in the plan could, by public announcement, be reduced. When, on the other hand, quantities in the plan had been fully contracted, the quantities first announced in the plan could again by public announcement be increased.

Alternatively, USDA could limit its annual announcement to a list of eligible EEP recipient countries. Such a step, while not preferable to the suggestion above, would provide improved transparency while also preserving USDA's flexibility to use EEP strategically for purposes of countering foreign unfair trade practices.

(6) THE BONUS SHOULD BE ANNOUNCED ON A DAILY BASIS AND THE SAME BONUS LEVEL SHOULD APPLY TO ALL ELIGIBLE COUNTRIES.

A weekly subsidy, such as used by the EC, might also be an acceptable alternative.

(7) UPON ACCEPTING A CERTAIN QUANTITY OF AN ANNOUNCED BONUS, THE EXPORTER SHALL DECLARE THE DESTINATION.

Unwarranted "nuisance" provisions of current regulations should be eliminated or reasonably amended. For example, qualification requirements currently deny participation to an exporter -- however financially sound and scrupulous its performance with government contracts may be -- simply on the basis that it has not, in the past, exported the commodity to be exported under a particular EEP initiative.

We have no interest in making eligible to participate in this program companies that are not properly eligible; nor have we an interest in loosening appropriate management safeguards. However, these requirements, as they apply to exporters currently participating in the program, appear to us to be anti-competitive and improperly exclusive.

Performance security requirements of EEP are needlessly burdensome. Once the financial capacity of an exporting company is established and, provided the company has a record of good performance on government contracts, the bonding requirements called for under current regulations should be waived for that company.

Likewise, regulations attending entry certification should be eased. In some cases it is difficult, if not impossible, to obtain evidence of entry in the form the regulations currently require. The regulations should allow in the alternative any competent and credible evidence such as certification by the vessel owner, any entity of the buyer's government in its country or in the United States, or a stevedoring firm, etc.. The purpose of the program is not to gather entry certificates of limited format -- it is to export grain.

Current program regulations should be amended to state that, in the event that a vessel sinks or a part of the cargo is lost, the bonus should not be forfeited.

Finally, exporters should not be penalized for failure to meet contract minimum when such failure is attributable solely to the presence of dockage. In accordance with international practice and freighting arrangements, the quantity stipulations of sales contracts provide that quantities are gross; i.e., including any dockage. CCC regulations should correspond.

The management proposals above have been submitted with particular reference to wheat. However, NAEGA notes that these proposals should be applicable to all commodities exported under the export enhancement program.

Senator **Boren**. Thank you very much. We appreciate your comments.

Mr. Fischer.

STATEMENT OF DUANE A. FISCHER, PRESIDENT AND CHIEF EXECUTIVE OFFICER, SCOULAR GRAIN CO., OMAHA, NE; TESTIFYING ON BEHALF OF NATIONAL GRAIN AND FEED ASSOCIATION, WASHINGTON, DC

Mr. **Fischer**. Mr. Chairman, the National Grain and Feed Association (NGFA) is pleased to be here today to discuss and offer specific recommendations concerning the 1990 farm bill.

INTRODUCTION

I am appearing today on behalf of the NGFA. We are very pleased that a measure of prosperity has returned to this Nation's farmers. Our industry has not yet shared in that recovery, as evidenced by the recent action by a major U.S. wheat exporter that posted "for sale" signs on all its U.S. grain operations. Grain companies large and small are struggling to shift their revenue generating functions from a storage driven to a market driven environment.

At present our industry has significant surpluses of underutilized grain handling capacity. In the two major grain producing and handling States of Oklahoma and Texas commercial storage capacity utilization ranges from 15 to 18 percent.

To ensure economic recovery is achieved in all sectors of agriculture, we believe the most important thing Congress can do in the 1990 farm bill is to set our Nation's agricultural policy on a sustained, steady course toward market orientation and growth with minimal reliance upon supply management or acreage reduction programs.

Given this objective, our policy recommendations concerning the 1990 Farm Act are designed to remove the obstacles in current law that impede the ability of our producers and grain merchandising industry to achieve our market potential and utilize our capacity.

NGFA Supports a Farm Policy Having the Following Objectives

PRODUCER PLANTING FLEXIBILITY

First, it is essential that the lack of planting flexibility in current law be addressed. Several constructive options are coming to the forefront. The normal crop acres concept proposed by the administration would address this problem. The same could be accomplished through a triple base or payment acres approach. The key point is to allow enough flexible acres to permit production to respond adequately to market signals.

ACREAGE REDUCTION POLICY

Second, acreage reduction policy adopted in the 1990 farm bill will be every bit as important as flexibility or price support loan rates in determining whether the United States is competitive in world grain markets. We submit that acreage reduction programs are a relic of a bygone era, a policy tool whose time has passed.

It is easy to lose sight of the fact that through a combination of ARP's, 0/92, the CRP, the United States in 1990 will idle 64 million acres. That is more than double the 31 million acres that were idled in 1985. We recommend the elimination of all ARP's and set-aside authorities. In their place a paid land diversion program would have the advantage of curbing the incentive to use ARP's as a method of reducing budget outlays.

REFOCUS THE CRP ON ITS ORIGINAL OBJECTIVE

Third, the 1990 farm bill provides Congress with an opportunity to refocus the CRP on its original objective. The wheat States have borne a disproportionate brunt of the CRP, with wheat comprising nearly one-third of the acreage enrolled. We fully concur with the administration's proposal to cap the CRP at 40 million acres and allocate remaining CRP acres to wetlands, seriously erodible lands, or acreage susceptible to ground water contamination. We also believe that once the 48 million acre cap is reached, it would be prudent to offer producers the option to enter into a "bid back" program in which they could return CRP land to production. Our proposal stems from the fact that many acres of productive farmland have been entered into the CRP, particularly in the early signup years.

I think, Mr. Chairman, what we foresee in that particular area is the chance to, within the 40 million acre cap, rotate more erodible acres into the program as we let better productive land out, and end up with just a better mix of acres in that program.

IT IS ESSENTIAL TO RETAIN MARKET ORIENTED LOAN RATE FORMULAS CONTAINED IN THE 1985 FARM ACT

Fourth, it is essential to retain market oriented loan rate formulas contained in the 1985 Farm Act. It took the U.S. Government half a decade to correct policy, even after it became obvious escalating loan rates were resulting in a precipitous loss of U.S. market share, a period formidable competitors used to launch major expansions of their agricultural production and infrastructure.

The difference between loan rates and world market competitive prices can evaporate quickly through changes in currency markets and macroeconomic policies by the United States and other nations. The temptation to raise loan rates or delete Findley authority for budgetary or any other reasons should be strongly resisted. The United States lost huge market shares by racheting up loan levels in the late 1970's and we should not make that same mistake again.

IT IS ESSENTIAL THAT GRAINS STORED IN THE FARMER-OWNED RESERVE BE MORE ACCESSIBLE TO THE MARKET

Fifth, it is essential that grains stored in the farmer-owned reserve be more accessible to the market. The administration's proposal is a step in the right direction, but with lower reserves it will be important to treat farmers equitably on entry of grain into the reserve. We favor a signup procedure in which producers can indicate to county offices the quantity of maturing loan grain they wish to enter into the reserve. USDA then could allocate a pro rata share to each producer if the reserve ceiling will be exceeded.

We also have misgivings over the use of annually changing farmer-owned reserve storage payments to producers as a means to attract or discourage entry of reserve grain. A modest reserve ceiling and greater accessibility to the market would adequately entice or discourage entry of grain into the reserve.

CCC'S CASH GRAIN SALES FORMULA SHOULD BE REDUCED

Finally, we believe, particularly in an era in which the supply and use of generic certificates will be more limited, CCC's cash grain sales formula should be reduced. CCC should be allowed to sell its inventories if prices are greater than 115 percent of the loan.

Mr. Chairman, we look forward to working with you and the subcommittee to ensure the 1990 Farm Act builds upon the market oriented foundation of its predecessor so prosperity can return to all sectors of the agricultural community.

Thank you.

[The prepared statement of Mr. Fischer follows:]

National Grain and Feed Association

Statement of the National Grain and Feed Association
by
Duane A. Fischer
Before the
Subcommittee on Agricultural Production and Stabilization of Prices
Senate Committee on Agriculture

March 8, 1990

Mr. Chairman and members of the Subcommittee, the National Grain and Feed Association is pleased to be here today to discuss and make specific recommendations on the components of the 1990 farm bill.

My name is Duane A. Fischer, and I am president and chief executive officer of the Scoular Grain Company, headquartered in Omaha, Nebraska, which operates country and terminal grain elevators and cash grain merchandising businesses in Nebraska and several other Western states. I appear today on behalf of the National Grain and Feed Association, on whose International Trade/Agricultural Policy Committee I serve. The NGFA is a voluntary association of grain and feed firms ranging in size from the smallest country elevator to the largest grain and feed complex. Our members represent a broad cross-section of America's grain and feed industry, which is comprised of country and terminal elevators, grain merchants, feed mills, processors and international exporters. Our members store, handle, merchandise and process more than two-thirds of all U.S. grains and oilseeds.

The NGFA commends the thoughtful deliberation this Subcommittee has undertaken in establishing a solid information base on which to make the crucial decisions for a policy framework under which America's farmers and agribusinesses will compete with their world counterparts during the 1990s. The prudent decisions made by Congress in the 1985 farm act went a long way by providing an economic environment that revived the ability of America's farmers and agribusinesses to be competitive in international markets. The decisions Congress is about to make concerning whether to continue the market-oriented transition that is the centerpiece of the 1985 act will determine whether the recovery that has begun in our agricultural sector will reach fruition in the years ahead.

No one could be more pleased than America's grain and feed industry that a measure of prosperity has returned to this nation's farm sector. Net cash farm income is projected to increase in 1990 to approach the 1988 record of $57 billion. In recent years, those net farm income returns have been generated increasingly from the marketplace, led by a resurgence in export demand for U.S. grains and oilseeds, which has increased an estimated 32 percent from 102 million metric tons in 1986 to 135 million metric tons in 1989.

While it is commendable that a period of improved net farm income has emanated from the 1985 act, our industry has not yet shared fully in that recovery. From the perspective of our industry, the 1985 farm act has resulted in a dramatic drawdown in Commodity Credit Corporation-owned grain inventories, which has depleted storage revenues upon which many elevators relied. As a result, all grain companies, large and small, are struggling to shift their revenue-generating functions from a storage-driven to a marketing environment. The increased revenues from merchandising high volumes of grain that inevitably will result from a market-oriented agricultural policy have yet to be fully realized by our industry, in part because of reduced grain volumes caused by the 1988 and 1989 droughts. Our industry still has significant surpluses of grain handling capacity. Indeed, in Oklahoma and Texas, two principal wheat-producing states, utilization of commercial storage capacity ranges from 15 to 18 percent, down from 30 to 40 percent utilization as recently as 1988-89.

Economic recovery of our industry is critically dependent upon having grains and oilseeds available in the volumes being demanded by the market. To ensure that economic recovery is achieved in all sectors of agriculture, the NGFA believes strongly that the most important thing Congress can do in the 1990 farm bill is to set our nation's agricultural policy on a sustained, steady course toward market orientation and growth, with minimal reliance on supply management or acreage reduction programs. To restore profitability to both the farm and agribusiness sectors, we need to produce, handle and sell grains. And all signs are that the world marketplace will be demanding ever-higher volumes of U.S. grains. For instance, feed grain utilization is projected to reach a record 239 million metric tons in 1989/90 marketing year, led by an 8 percent increase in exports to 66 million metric tons -- the highest level since 1980-81.

Given this objective, our comments relating to the 1990 farm act are designed to remove some obstacles that exist in current law that impede the ability of our producers and grain handling and merchandising industry to achieve our market potential. Cognizant of this overall goal, the NGFA supports a farm policy having the following objectives:

- Promote a competitive marketplace worldwide that will ensure the most efficient production and marketing system possible.

- Ensure that price support, income support, production controls and other facets of domestic farm programs do not interfere with the United States' ability to compete in international markets. Farm programs should not inhibit the productive capacity of efficient U.S. farmers.

- Provide each producer with the freedom to choose which crops, and in what volumes, he or she wishes to produce, thereby increasing the ability of U.S. agriculture to produce in response to market signals, not because of the dictates of government farm programs.

- Encourage the development and maintenance of U.S. export market programs, including short- and long-term credit programs to food and feed industries that have the greatest long-term positive impact upon demand for food and grain.

- Promote the reduction or removal of international tariffs and nontariff trade barriers that limit the international trade of grains, oilseeds and their products; and

- Encourage the use of food aid programs for relief purposes and market development of U.S. grains and oilseeds in other countries.

Let me now turn to specific recommendations on components of the 1990 farm bill.

Producer Planting Flexibility

From our standpoint, planting flexibility is a central element of true market-orientation: Allowing farmers to plant the crop demanded by the marketplace rather than in response to the dictates of federal farm programs. This factor may be the most critical to be addressed in the 1990 farm bill. The dramatic shift in U.S. acreage from oilseeds to corn since passage of the 1985 farm act, despite increasing demand for oilseeds and oilseed products, demonstrates that inflexible acreage base systems are incompatible with the needs of the marketplace. Since 1980, the United States has abdicated approximately 10 million acres of oilseed production. These acres have not been lost on a global scale, however. During this same period, plantings of soybeans, sunflowerseed and rapeseed have risen 7 million acres in the European Community and by 19 million acres in the Southern Hemisphere.

The ultimate impact of this production shift has been a loss of U.S. competitiveness and a decline in America's ability to meet market demand. If this trend is not halted and reversed, the United States soon may find itself in the position of importing oilseeds to meet domestic crushing demand.

Clearly, producer decisions to plant corn instead of an alternative crop were driven by considerations other than market demand — a major policy issue that we believe Congress must address in the 1990 farm bill.

Permitting the market to give production signals to producers also helps minimize the risks of temporary market shortages related to early farm program announcements. Program announcement dates are often 12 months in advance of harvest so there is considerable potential for error in estimating supply needs. The impact of any error perhaps would have the greatest repercussions for wheat, since the approximately 443 million bushel carryout projected for the 1989/90 marketing year equates to only 70 days supply for domestic and export use. Allowing the market to send price signals that affect planting decisions near planting dates will help the United States maintain adequate supplies of all major commodities and preserve our competitiveness.

In addition to the loss of market competitiveness, the current lack of flexibility in farm programs has seriously discouraged producers from exercising sound soil management practices. This could portend disturbing implications for the future. In the 1985 act, Congress devoted considerable resources to soil conservation and environmental issues. The Conservation Reserve Program is but one tangible aspect of these efforts. Environmental issues will continue to be crucial agricultural concerns. But the rigid crop base structures and payments run counter to good soil management practices because they discourage, for even one crop cycle, any rotation to other crops.

Options For Flexibility

In a perfect environment, true planting flexibility would allow farmers the freedom to base production decisions primarily on market prices and technical factors that affect the physical function of a farm, such as conservation practices and environmental considerations. However, many proposals discussed thus far in the 1990 farm bill debate do not envision such an environment. They either limit the planting of alternative crops or contain immediate or potentially delayed penalties to the producer's base and/or income protection.

However, several constructive options for addressing the flexibility issue now are coming to the forefront. Strictly from the viewpoint of providing the farmer with adequate acres on which to plant crops of choice, the National Grain and Feed Association believes the Normal Crop Acres (NCA) concept proposed by both the administration and Sens. Lugar and Leahy (S. 1926) is an attractive option. These proposals would provide producers with adequate ability to match production with market signals with relatively few restrictions. Moreover, the administration's proposal would provide income support to producers wishing to plant alternative crops and would not penalize the producer through an immediate loss of crop base.

A potential inequity inherent in the NCA approach, which has received some discussion but few corrective recommendations, is the potential loss of price support for the producer with small crop acreage bases for wheat, feed grains, cotton or rice but who grows primarily soybeans or other nonprogram crops.

The NGFA believes Congress should closely examine this issue if an NCA approach is adopted as part of the 1990 farm bill, but offers no specific recommendations since our members are not beneficiaries of price and income supports.

The NGFA also believes a "triple-base" or "payment-acres" proposal, if properly structured, would provide producers with the freedom to better respond to market, environmental and conservation signals. However, we caution that a triple-base program should provide farmers with adequate flexibility to shift reasonable amounts of acreage to alternative crops. A producer's flexible acreage should not be linked to a formula that would offer only minimal available acreages for alternative crop production.

Acreage Reduction Programs/Conservation Reserve Program

The decision to idle highly productive U.S. farmland in the immediate aftermath of the 1985 farm act was a fairly easy decision for U.S. policymakers to make given the existence of heavy inventories of CCC-owned grain accessible with generic commodity certificates that would serve as a supply buffer to meet market demand. The grain surpluses allowed USDA to continue large acreage reduction programs mainly as a means to control federal budgetary exposure.

But that luxury is over. In just the last two marketing years, wheat carryover declined from

1.261 billion bushels to 443 million bushels by the end of the 1989/90 marketing year. Corn carryover declined by more than half, from 4.259 billion bushels in 1987-88 to 1.48 billion bushels in 1989-90. Carryout stocks of wheat, rice and corn in all of the major exporting nations also declined precipitously. The United States is extremely short of soybean supplies and continues to import basic commodities like oats.

Simply put, policymakers no longer can ignore the supply needs of the market when devising the type of acreage reduction programs that will influence U.S. supplies in the future.

The NGFA believes that the acreage reduction policy adopted in the 1990 farm bill will be every bit as important as planting flexibility or price support loan rates in determining whether the United States will be competitive in world grain markets in coming years. Increasingly, we submit, acreage reduction programs are a relic of a bygone era -- a policy tool whose time has passed. Few, if any, nations in the world hamstring their producers or their marketing infrastructure to the extent the United States still does with acreage reduction programs.

There are a host of factors that make a compelling case for less reliance on acreage reduction programs:

■ First, acreage reduction programs reduce the efficiency of the agricultural sector. They idle productive resources that have few alternative economic uses. Fixed costs of resources and infrastructure must be paid for through smaller volumes of output, adding to the costs of producing each bushel. According to the Agricultural Policy Working Group, a 20 percent set-aside program can add as much as 33 cents per bushel to the production costs of a typical Iowa corn farmer. Production controls affect members of the National Grain and Feed Association and those who ship, process and export U.S. grains, as well, by keeping productive capacity in these segments of the marketing chain from being utilized fully or at their peak efficiency. Further, a finely tuned U.S. agricultural marketing and transportation infrastructure -- one of this nation's true competitive advantages -- cannot serve at maximum efficiency if it is placed on idle. The end result is a higher unit cost for producing and exporting U.S. agricultural products. For these reasons, acreage reduction programs work heavily against us as we strive to be the most efficient, competitive nation in agricultural commodity production and marketing.

■ Acreage reduction programs encourage foreign production and competition. History provides ample evidence that when the United States limits output, foreign competitors are encouraged to clear land and expand production to displace what otherwise would be U.S. sales. Perhaps this was demonstrated most graphically in the 1983 payment-in-kind program, when the 77 million acres of idled U.S. farmland were replaced virtually acre-for-acre by foreign plantings. Importantly, when this kind of signal is sent to our foreign competitors, they gear up not only their grain production capacity, but their storage, transportation and marketing infrastructure, as well, undermining the United States' strong comparative advantage in this vital aspect of our overall competitiveness.

■ Acreage reduction programs limit market growth and promote development of substitute products. Limiting production can restrict the availability of a commodity and cause users to look elsewhere for cheaper alternative products.

■ Acreage reduction programs can lead to international trade confrontations resulting from a lack of CCC stocks to combat unfair trade practices. U.S. policymakers, particularly in the Export Enhancement Program for wheat, confront a situation in which the rapid drawdown in U.S. wheat stocks has reduced the number of export enhancement offers and the quantity of wheat than might otherwise have occurred.

Yet, despite these multiple factors, the 1985 farm act currently provides USDA with no less than five acreage reduction authorities -- the traditional ARP, the 0/92 program, the paid land diversion authority, the Conservation Reserve Program and the emergency mid-year set-aside authority and cost-reduction options granted under Section 1009 of the 1985 farm act. Given the use of these combined authorities, we sometimes lose sight of the fact that the United States continues to idle vast amounts of productive farmland. In fact, for the 1989 crop year, it was projected that through the use of ARPs (18.5 million acres), the "0/92" set-aside program (11.4 million acres) and the conservation reserve (34 million acres), the United States idled nearly 64 million acres of farmland, more than double the 30.8 million acres idled in 1985, the last year before 1985 farm act.

It can be argued that acreage reduction programs have been used recently more as a budget-control measure than as a supply-management tool. Cognizant of the detrimental impacts of acreage reduction programs, the NGFA believes that their use for budget purposes is poor public policy. If budget outlays continue to warrant action by Congress, perhaps the focus should be shifted to ways to limit ASCS payments rather than increasing production costs for agriculture through the use of relatively high, non-market-oriented set asides.

There is another factor that serves as a caution flag when it comes to establishing acreage reduction levels. Past experience has provided ample evidence of USDA's difficulty in accurately or precisely projecting actual crop carryover levels as far in advance as is required when announcing farm programs for the coming year. For planting purposes, it is important to provide producers with ample lead time by announcing the elements of the coming year's farm program well in advance. But when doing so, USDA historically has overstated the size of crop carryout in the United States and the world, and established an acreage reduction requirement based upon those overestimated levels.

Acreage Reduction Recommendations

Given these factors, the NGFA recommends the elimination of all acreage reduction and set-aside authorities. If Congress believes it is necessary to attempt supply management through a type of set-aside program, a paid land diversion would have the considerable advantage of curbing the incentive to utilize acreage reduction programs as a method of reducing federal budget outlays. Realizing that ARPs have been used for the wrong reasons -- i.e., as a budget-cutting tool rather than as a supply-management mechanism -- we believe providing the secretary of agriculture with the authority to instead implement paid land diversion as an alternative for deleting ARP authority would have merit.

Our fundamental opposition to granting the secretary of agriculture the authority to implement ARPs causes the NGFA to oppose the administration's 1990 farm bill proposal to grant the secretary triggered ARP authority. We also believe that the percentage levels of acreage reduction sought in the administration's proposal based upon stocks-to-use-ratios for wheat and feed grains are too high, especially considering the United States already has removed 34 million acres under the Conservation Reserve Program.

We also oppose the continuation of the so-called "0/92" program, which hits hardest at the rural communities located in areas with large concentrations of farmland entered into the Conservation Reserve Program. Moreover, in years of lower market prices, large participation in the "0/92" program can affect U.S. agriculture just as adversely as any other massive acreage reduction program.

Finally, it is important to recognize that while its objectives are laudable, the Conservation Reserve Program also has left a considerable imprint upon the landscape of rural America by idling vast amounts of farmland, some of it relatively productive. And it should be noted that wheat has borne a disproportionate share of the brunt of CRP. Of the total 34 million acres enrolled in the CRP, nearly 10.3 million acres have been wheat. The five states of Colorado, Kansas, Nebraska, Oklahoma and Texas have seen nearly 4.4 million acres of wheat enrolled into CRP. At current rates of enrollment, it will be very difficult for USDA to meet the congressionally mandated minimum target of 40 million to 45 million acres for the Conservation Reserve Program by the 1990 crop year. We believe strongly that productive farmland should not be enticed into the CRP by relaxing soil-loss criteria or increasing rental payments to exorbitant levels to achieve mandated minimum levels of entry. Given the current situation in grain and oilseed stock levels, to alter such criteria would be to shift the CRP into another form of long-term production control device rather than as a protector of the nation's natural resources.

The NGFA recognizes the desirability and need to remove environmentally fragile farmland from production. We fully concur with the administration's proposal to place a maximum ceiling of no more than 40 million acres on the size of the Conservation Reserve Program, and to refocus the remaining acres to be entered into the reserve on wetlands or other environmentally sensitive lands, particularly areas susceptible to groundwater contamination.

But we believe the 1990 farm bill provides an opportunity for Congress to refocus the Conservation Reserve Program on its original purpose -- as a safe haven for land that meets the most severe erodibility criteria or is truly environmentally threatened. Unfortunately, that has not always been the case in the method with which the CRP has been implemented. There have been instances in which highly productive farmland has been enrolled in the CRP, particularly in the early signups, when CRP payments were very attractive compared to cash rent or crop share rent prospects.

In addition, too often individual counties have been allowed to exceed the ceiling of 25 percent of acreage that under normal circumstances is to be the maximum allowed into the CRP. USDA reports that no less than 80 counties currently have anywhere from 25 percent to 50 percent of their base farm acres locked up in the CRP. In several instances, this additional land has been enrolled into the CRP with only cursory consideration given as to the adverse -- and in some cases debilitating -- impacts on local businesses and the economic lifeblood of rural communities, a requirement that Congress mandated be assessed when creating the CRP in the 1985 farm act. In some cases, our members have informed us that they have been approached by ASCS county officials and, in action that borders on intimidation, informed that if they did not concur to have the additional land idled they would face the prospect of having their names identified to local farmers who wanted to have their acreage enrolled in the CRP. In still other cases, as members of this body are all too aware, members of Congress have been placed in the untenable position of being arbiters in deciding whether individual counties should be allowed to exceed the 25 percent threshold on enrollment into the CRP.

Options for CRP

Suffice it to say there are indications some relatively productive, flat, rolling farmland has been enrolled into the CRP that given current grain supply-and-demand projections is better suited to being used for agricultural production. Likewise, no doubt there are some environmentally fragile lands still being used for production that may be deserving of entry into the CRP. To address these concerns, we strongly recommend that Congress consider adopting two changes to the CRP.

■ First, we believe future enrollment in the CRP should be limited to those acres that meet the most serious erodibility criteria established by the Soil Conservation Service. These criteria that determine eligibility of land to be enrolled in the CRP were eased before the sixth sign-up period in February 1988 to twice the normal soil loss tolerance level rather than the previous requirement of at least three times the normal soil loss tolerance level. In addition, to enroll a field in the CRP, previously at least two-thirds of the field must have been classified as highly erodible. But beginning with the sixth signup, only one-third of a field must contain highly erodible soil if it will be planted to trees. Further, USDA's maximum acceptable rental rates were increased after the sixth CRP sign-up period. The net result is that our country elevator segment has witnessed some relatively productive farmland being enrolled into the CRP -- farmland that could be restored to production if proper conservation compliance plans are implemented.

■ Second, we believe once the 40-million-acre target for the CRP is attained, it would be prudent to offer producers the option to enter into a bid-back program in which they could return to production that land previously entered into the CRP. The bid required from the producer could be set at a level that compensates USDA for the 50 percent share that taxpayers paid to the producer to establish a cover crop on the CRP acres. From an environmental standpoint, this concept also has merit. For one, these CRP lands that farmers successfully bid back into production still would be required to meet "T" values established by the Soil Conservation Service as part of the producer's individual conservation compliance program. This would ensure that any CRP land restored to production would meet specific erodibility criteria. Second, productive farmland bid-back into production under this concept would make room for more fragile or highly erodible lands that may deserve entry into the CRP.

Loan Rates

Prior to enactment of the 1985 farm act, the United States operated a non-recourse loan program that set minimum prices at high levels which were downwardly inflexible. This was viewed as a "low-risk" policy in the mid- to late-1970s, when the United States experienced a strong demand for exports that escalated farm commodity prices. The government increased price support loan level floors simultaneously, such that they rose from $1.37 to $3.65 per bushel for wheat and from $1.10 to $2.65 per bushel for corn during the period of 1975-83. As recently as 1980, this ratcheting upward of loan rates still was viewed as minimal risk, since at the time average wheat market prices still were 30 percent greater than the loan rate, while average corn market prices were 38 percent more than the loan level.

But market conditions of the early 1980s changed dramatically, with the increasing value of the dollar and the entrance of new competitors into the international marketplace. In less than two years, loan rates for both wheat and corn were creating substantial barriers to U.S. market competitiveness and providing America's competitors with significant protection against world price declines.

Through excessive loan rates, U.S. agricultural policy actually stimulated our foreign competition. Under U.S. farm policy of the early 1980s, many foreign countries became very comfortable in expanding production by leaps and bounds. As long as world production remained at fairly reasonable levels, U.S. loan rates provided an insurance policy that the United States would unilaterally act to control supply and raise prices in following years through set-aside programs if prices declined to less than the loan rate.

The National Grain and Feed Association and others called on Congress to implement a more market-oriented loan program as a cornerstone for returning prosperity to U.S. agriculture and rural America. After much debate on the issue, Congress wisely included in the 1985 act provisions mandating reduced loan levels and provided the secretary of agriculture with discretion to reduce those rates even further, if necessary, to ensure they remained consistently below market-clearing levels.

World grain exporting nations took notice and confronted new risk when considering bringing additional land into production. From 1981 to 1987, total world harvested acreage for grains and oilseeds declined from 860 million to 820 million hectares. It is impossible to calculate how much of this decline can be attributed to U.S. policy changes; but it is reasonable to believe that such policy changes had a tremendous impact on global production decisions.

Options For Loan Rates

Because of its demonstrated success, the National Grain and Feed Association strongly supports the continuation of the current U.S. policy of a market-oriented loan program. We oppose any attempt to remove the secretary of agriculture's discretionary authority to implement the Findley provision to lower loan rates by an additional 20 percent, if needed, to remain competitive in the global marketplace. We believe it would be extremely shortsighted to remove such an authority for purposes of budget savings or any other reason.

Recent history provides ample evidence of the importance of retaining the current policy course concerning price support loan rates:

First, even after it became obvious that the level of price support loan rates were resulting in precipitous losses in U.S. market share, it took the U.S. government half a decade to respond by reversing the upward trend in loan rates and thereby helping restore U.S. competitiveness in world markets. But during the intervening years, the United States provided an unchallenged opportunity for some formidable competitors to launch major expansions of their own agricultural production and infrastructures.

Second, it is difficult to project a "comfort zone" when it comes to the relationship between price support loan rates and market prices. Wheat market prices exceeded the loan rate by 51 percent in 1979 while corn market prices exceeded the loan rate by 38 percent in 1980. Yet, in less than two years those "comfort zones" -- the difference between market prices and the loan rate -- had evaporated to zero.

A situation reminiscent of the 1979-80 period existed in the difference between loan rates and market prices in 1989, when the drought-impacted wheat market prices exceeded the loan rate by 87 percent, while corn prices exceeded the loan by 33 percent. In a more normal weather year with adequate wheat stocks and a more normal export market share for U.S. wheat, wheat market prices probably would not exceed the loan rate by more than 50 to 60 percent. Thus, the current differential between world market-competitive price levels and loan rates are very similar to that experienced in the late 1970s, when the United States became overconfident that it could increase loan rates and still be immune to risking its market share. Similar conditions that occurred during the 1980s could again develop in the 1990s, as world financial markets are subject to wide swings in international capital flows resulting in fairly unstable world markets for currency. Depending upon monetary and fiscal policies of major world economic powers like the United States, Japan and Germany, the value of the dollar could escalate again. Such an occurrence could quickly change the relationships between market prices and loan levels experienced in U.S. markets and remove the "comfort zone" that now appears to exist between U.S. loan rates and market prices.

Third, as has been demonstrated since the mid 1980s, increasing loan rates, no matter how superficially, provides a "comfort level" signal to our international competitors. Put simply, higher U.S. loan rates reduce the perceived risk our competitors have in investing more capital to expand their own agricultural infrastructures. Any investor assessing alternative opportunities will be encouraged to invest more in those enterprises that offer the least risk.

As exporters of U.S. grains and oilseeds, we can attest to the increased volatility and uncertainty of the global marketplace. This environment has changed dramatically from the 1970s, when the United States was the dominant exporter.

Today, with many exporting nations competing fiercely for markets and the value of the dollar fluctuating dramatically, Congress and the administration can ill-afford to attempt to adjust loan rates within a narrow margin to market prices without running a great risk to our competitiveness. If the United States is to continue a loan program as part of a market-oriented agriculture, procedures for establishing loan rates must ensure that loan levels do not interfere with market-clearing mechanisms. The current formula for computing loan levels works well and should be continued, provided the secretary of agriculture continues to have discretionary authority to impose the "Findley" provision and lower loan levels when needed for the United States to remain competitive. Unfortunately, the U.S. government could resume its position as the market for U.S.-produced grains and oilseeds if the Findley authority is removed from current law.

Also for the reasons mentioned above, the NGFA recommends that a ceiling be placed on the extent a loan rate could increase from one year to the next. Just as current law prohibits the formula from reducing the loan rate by more than 5 percent of the previous year's level, we believe that the rate should be able to increase by no more than an equivalent amount of 5 percent compared to the previous year.

Farmer-Owned Grain Reserve

In the continued pursuit of a more market-oriented agricultural policy, changes to the operation of the farmer-owned reserve are needed. This is particularly the case since it appears that with the drawdown in CCC inventories, the major tool that the market used to access stocks from the reserve in the past four years -- generic certificates -- will play a much more limited role in coming years. With it, the structural impediments inherent in the existing farmer-owned reserve program and CCC's cash sales policy will be magnified.

During the past decade, the farmer-owned reserve program has been used for two distinct purposes. The first has been to supplement farm income, both through "premium" reserve loan rates in some years and through advance storage payments to producers. An ancillary effect has been that these FOR stocks have been "isolated" from the market to artificially prop up prices. However, the market always "knew" those stocks were there, which had the effect of dampening what otherwise would have been more immediate and dramatic grain price increases during periods of greater demand and lower production. The second purpose has been to maintain adequate supplies for food security and to undergird the United States' reputation as a dependable source of supply.

Unfortunately, these two objectives of the FOR can and have worked at cross purposes with one another, frustrating both the intent of Congress and the needs of the marketplace for grain. The recent history of the FOR reveals that during periods when the market needed access to the stocks enrolled in the FOR to respond to increased demand, stocks could not be acquired readily. That action to isolate U.S. stocks from the marketplace became yet another signal to our foreign competitors to increase production and become more aggressive in their exports, safe in the assurance that the United States would not encourage producers to redeem grain from the FOR.

The FOR also has been unpredictable, plagued by frequent program changes that have hampered its dependability. Too often, abrupt changes have been made in the rules governing the reserve to serve short-term government objectives. Such rule changes tend to be highly disruptive to an orderly marketing system, and should be discouraged.

The NGFA believes that a prudent grain stocks policy should be founded on two basic principles:

■ First, the need to maintain a food security reserve and meet humanitarian needs. In this regard, it is important to recognize the FOR does not shoulder the sole burden for fulfilling emergency needs. Rather, it is part of a wider strategic reserve that also consists of a 147-million-bushel Emergency Food Security Reserve and a 75-million-bushel Disaster Reserve consisting of feed grains.

■ Second, to ensure that the United States remains a reliable source of supply to meet market demand.

One of the biggest problems with the farmer-owned reserve is its current release levels. Set at the target price for the respective commodity, they are both too high and too inflexible to be responsive to market demand. The past several years are replete with situations illustrative of problems posed by FOR release levels.

An excellent case-in-point is found in the wheat market. USDA estimates that at the end of the 1989-90 marketing year, the United States will hold 494 million bushels of wheat. Of that, 150 million bushels will be enrolled in the FOR, representing roughly 30 percent of the total.

This wheat will be very difficult for the market to access, especially if generic certificates are in relatively short supply. Consequently, at the end of the wheat marketing year, there will be approximately 350 million bushels of wheat readily available to the cash markets to respond to demand. There also have been situations in which selected classes of wheat have been imported to meet domestic milling needs, even while some quantities of the same classes of wheat remained isolated in the FOR.

There are similar examples in the case of feed grains. In corn, the severe 1988 drought significantly reduced stocks and caused prices to escalate sharply. Despite this obvious market signal for grain, and despite the fact that generic certificates were relatively plentiful, very little corn was liquidated from the FOR, with 740 million bushels remaining in the reserve at the end of the 1988 crop year.

But perhaps the classic example occurred in 1983, when a major acreage reduction program -- the infamous Payment-in-Kind program -- and a subsequent drought combined to reduce corn stocks significantly. Although cash market prices increased to levels well above release levels, nearly 450 million bushels -- representing more than 44 percent of the total corn carryout -- remained in the FOR at the end of the crop year.

Such examples provide ample evidence that stocks indeed can become "trapped" in the FOR, with market prices needing to rise to levels so excessive that alternate sources of grain supply can be found and demand for U.S. grains can evaporate before such prices are attained.

FOR Policy Recommendations

When analyzing the mechanism governing release of FOR stocks, it is important to recognize incentives that influence a farmer's decision whether to market reserve grain.

Currently, producers receive storage payments for their FOR grain one year in advance. Should producers wish to market their reserve grain, any unearned storage must be repaid. Consequently, producers must factor in the cash-flow aspect of repaying unearned storage -- an obvious financial and psychological barrier -- compared to the market price to be received.

To remove this built-in disincentive in the future, the NGFA believes Congress should consider mandating that storage payments for reserve grain be made in a manner similar to that used for commercial elevators storing CCC-owned grain under the Uniform Grain Storage Agreement contract -- namely, that payments be made quarterly after the grain has been stored for a three-month period.

Another option we believe warrants consideration if the FOR is to be made more responsive to market orientation is to eliminate the penalties a producer must pay when marketing grain that is not in "release" status. The promise of receiving storage payments remains a strong incentive for producers to keep grain enrolled in the FOR. But elimination of penalties for sale at less than the release level would allow some FOR stocks to come to market to meet demand needs in a more orderly way.

A third option that the NGFA believes is necessary if FOR stocks are to be made generally more accessible to the market is to set FOR release levels at no greater than 140 percent of the county ASCS price support loan rate. We believe such a release level will encourage producers to carry stocks forward if they perceive the marketplace is signaling them to do so without isolating such stocks from the market indefinitely. Under current market conditions, the FOR would continue to be in release status -- an appropriate status given current demand for such stocks.

Our policy recommendations concerning the farmer-owned reserve differ on some of the specifics, but philosophically are in concert with those contained in the administration's 1990 farm bill proposal. Concerning the administration's concept of offering annual FOR contracts subject to renewal, with a 600-million-bushel ceiling for feed grains and 300-

million-bushel cap for wheat, we offer two thoughts:

■ First, it will be important under such a concept to treat farmers equitably concerning entry of maturing price support loan grain into the reserve. We tend to favor a sign-up procedure similar to that used for the 10/25 soybean program. Under this concept, producers could indicate to county ASCS offices the quantity of maturing loan grain they wish to enter into the reserve, with USDA to pro-rate the quantity each producer is allowed to enter if they designate quantities that exceed the reserve ceiling levels. This would avoid a situation in which producers rush to the county office on a first-come, first-served basis at the start of the marketing year to enroll grain in the farmer-owned reserve.

■ Second, we have some misgivings over the use of a varying storage payment level set annually by USDA as a means for attracting or discouraging entry of grain into the reserve. It appears to us that a reserve quantity with a relatively low ceiling and greater accessibility to the market (with a lower release price, or even no specific release price as called for in the administration's proposal) would serve as adequate controls for enticing or discouraging entry of grain into the reserve.

■ Third, generally we believe the size of the farmer-owned reserve should be modest. However, the maximum levels of the reserve are somewhat dependent upon the accessibility producers and the market would have to reserve stocks. We are further evaluating the administration's proposal in this regard, and would like to share our recommendations with you in the near future.

CCC Grain Sales Policies

Prior to the new era ushered in by the 1985 farm act and the generic certificate program, CCC-owned inventories also were isolated from the marketplace by an overly restrictive sales policy. Those minimum CCC cash sales prices -- which dictate that grain cannot be sold for cash at levels less than 110 percent of the current respective FOR release level -- remain in effect today for commodities for which a reserve is established. The only way CCC can sell its grain at market values for cash is for the grain to go out of condition to the point that it can be sold as “non-storable” -- defined currently as grain that is U.S. No. 3 because of damage or U.S. No. 4, 5 or sample grade.

These CCC cash sales levels are much too high, particularly if the generic certificate program is diminished and the market once again needs to use cash to obtain title to CCC-owned grains. Consequently, the same problems resulting from artificial “isolation” of government- owned or controlled stocks from the marketplace that exist in the current FOR also apply to CCC's cash sales policy.

To correct this problem, the NGFA recommends that CCC be authorized to sell its inventories for cash whenever prices are greater than 115 percent of the national adjusted loan rate for the respective commodities. As alluded to previously, this policy change is particularly important given the prospect that the availability of generic certificates will become increasingly tight. Reducing the statutory sales price will provide the secretary of agriculture with the ability to allow access to CCC-owned stocks when market demands dictate.

Emergency Reserves

Some have recommended that the 147-million-bushel "Emergency Food Security Wheat Reserve" should be combined with the FOR and be stored on-the-farm. We strongly oppose such an idea. By its very nature, the Emergency Food Security Wheat Reserve is designed to supply wheat for the P.L. 480 food aid program or other humanitarian needs as deemed necessary. Frequently, access to stocks stored in this emergency reserve is needed quickly. As such, it is paramount that wheat stocks designated for the Emergency Food Security Wheat Reserve be stored in commercial channels readily accessible to the grain pipeline so that they can reach export terminals in a timely manner.

The same rationale holds true for the 75-million-bushel Disaster Reserve comprised of feed grains. To store either of these emergency food and feed reserves in out-of-position locations would defeat their purpose and would greatly increase the costs of these programs while posing logistical nightmares in responding expeditiously and effectively to emergency needs.

Further, while we do not support a government policy that concentrates ownership of large quantities of stocks by the government, these particular food and feed aid programs justify moderate stock holding by CCC.

Conclusion

Mr. Chairman, we appreciate this opportunity to provide our thoughts concerning this most important piece of legislation. We look forward to the opportunity to work with you and this Subcommittee to ensure that the 1990 farm bill builds upon the market-oriented foundation laid by the Food Security Act of 1985 and the solid progress that has ensued since then so prosperity can return to all sectors of our agricultural production and marketing industry.

Senator BOREN. Thank you very much.

Let me ask just one final question of the group. Several of you mentioned the manner in which the Export Enhancement Program has been administered contributing to some instability in pricing and so on, and you mentioned you hoped for improved ways of administering the Export Enhancement Program.

Could you comment, the ones of you that mentioned that or wish to comment on it, on that a little more in detail in terms of constructive suggestions you would have for how we could change the way in which the EEP is being administered now?

Mr. MARTEN. I think maybe there are a couple of points to be made. One might be that it is certainly the perception of those of us a bit west of here that there is indeed a quote-unquote "grain board" that is operating, and we look at supply and demand statistics with somewhat of a grain of salt because we know that the Export Enhancement Program can be managed such that that ending stock number can be whatever the Government wishes it to be. That is point number one.

Number two is simply an appearance of arbitrary announcements of quantities. I would much rather operate in a free market environment where the individual grain companies have the opportunities to make sales and, you know, granted those may be surprises, but again, treating the Government as a partner in the process rather than necessarily an enemy, and when the Government makes large bonus announcements that radically affect the market, that is both negative for consumers and the producers, and again, not to belabor the point, but wanting the Department of Agriculture and the Government to be a partner in that process.

Senator BOREN. Thanks. Any other comments?

Mr. LYONS. Steve McCoy, president of NAEGA is here, and he may want to comment. But I would just like to say I think it is a situation where you don't have the buyer and the seller, in a sense, talking directly to each other. You have the buyer talking to USDA. Then the buyer comes forward to give the price to the seller. Then a bonus proposal is put together by the seller and it is sent to USDA.

There is no discussion between the buyer and the seller on price, class of wheat, any of those kinds of things. So it is a situation where there is not openness, not transparency, whatever you want to call it. That is one of the real difficulties with it.

Senator BOREN. Mr. McCoy, do you want to comment?

Mr. MCCOY. Thank you, Mr. Chairman. I would just mention that the exporters have put forward a fairly lengthy discussion of these issues which is appended to the testimony. You might want to take a look at it. [See pp. 349-352.]

Senator BOREN. All right. Good. I appreciate that and we will do that.

Again, thank all of you for being here. I apologize that we kept this panel as late as we did. We had thought we would have had you on about an hour before, but I think it is due to the interest of the members, and particularly as we were questioning the witness from the Department. It just went on longer than we expected, but it is an indication of interest in this whole area of policy.

We appreciate your patience, appreciate you remaining with us to the end. I assure you my colleagues will be studying this testimony with great interest, because as you could tell in the beginning, there is great interest in this section of the bill as we are going to start to work on it.

We expect to move out pretty quickly, let me say too. I know, talking with Chairman Leahy, that we expect not to let this process drag along, but we hope to break some records this year in terms of getting the farm bill written much earlier than usual.

In fact, we might even be revolutionary enough to let it be early enough that some people could make some decisions based upon knowledge of what the program is, which would indeed be a revolutionary change. But we are going to do our best to do that.

Thank you all again for being with us, we appreciate it very much.

[Whereupon, at 5:10 p.m., the subcommittee recessed to reconvene at 2:10 p.m., Thursday, April 19, 1990, in room SR-332, Russell Senate Office Building.]

PREPARATION FOR THE 1990 FARM BILL

Deficiency Payment Problems Associated With Barley Production

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THURSDAY, APRIL 19, 1990

U.S. SENATE,
SUBCOMMITTEE ON AGRICULTURAL PRODUCTION AND
STABILIZATION OF PRICES OF THE
COMMITTEE ON AGRICULTURE, NUTRITION, AND FORESTRY,
Washington, DC.

The subcommittee met, pursuant to notice, at 2:10 p.m., in room SR-332, Russell Senate Office Building, Hon. David H. Pryor (chairman of the subcommittee), Hon. Max Baucus presiding.

Present or submitting a statement: Senators Baucus, Boschwitz, and Gorton.

Also submitting a statement: Senator James A. McClure.

STATEMENT OF HON. MAX BAUCUS, A U.S. SENATOR FROM MONTANA

Senator BAUCUS. Welcome to today's hearing.

The droughts of 1988 and 1989 curtailed barley production in our country. As a result, Feed barley producers have become acutely aware that the formula used to calculate the barley deficiency payment is seriously flawed.

Currently, the USDA calculates the target price based on the relative feed value of barley to corn. However, the USDA then calculates the market price based on the feed value of barley *and* the higher-valued Malt barley.

Barley used for malt carries a premium market price which normally runs at about $0.25 to $0.35 per bushel and has only a minor effect on average market price of barley.

However, due to a short crop in 1988, Malt barley market prices skyrocketed to $3.24 per bushel, as compared to $2.29 per bushel for Feed barley.

Consequently, the USDA calculated the national average market price for barley as a whole to be $2.83, or $0.32 per bushel above the Feed-barley-only-based target price of $2.51.

This inequitable calculation places Feed barley producers at a unique disadvantage and is unfair. They are required to repay the entire advance deficiency payment even though they didn't get anywhere near the USDA's calculated market price for their barley.

The USDA should be consistent when figuring target prices and market prices for barley.

Either the USDA should use the malting value of barley in calculating the target price for all barley and keep them combined when determining the market price for deficiency payment purposes; or the USDA should continue its practice of separating Feed barley from Malting barley when determining the target price, but separate the two *also* when figuring the market price.

This way, Feed barley and Malting barley would be treated completely separately for income support purposes, or completely together. Not separately in one instance when figuring target prices and together in another instance when figuring market prices.

The effect of USDA's inequitable calculation hits barley producing States hard.

If we don't fix this problem, 16,400 barley producers in Montana alone will have to repay $19 million in advance deficiency payments for 1988. And 13,200 Montana producers will have to repay $6.75 million for 1989.

The problem is so serious in my State, in fact, that in recent weeks I have received two petitions urging congressional action to correct this problem. One is from Teton County containing 196 signatures. Teton County stands to lose over $1 million if the problem is not solved. The other is from Women Involved in Farm Economics and contains over 500 signatures.

The purpose of this hearing is to figure out the best way to fix the problem so that Feed barley producers will not be penalized by a flawed formula used to calculate deficiency payments.

I look forward to your testimony.

I will insert the prepared statement of Senator McClure, without objection, at this point in the hearing record.

PREPARED STATEMENT OF HON. JAMES A. MCCLURE, A U.S. SENATOR FROM IDAHO

HEARING ON BARLEY DEFICIENCY PAYMENT PROBLEMS

Mr. Chairman: I appreciate the opportunity to bring to the committee's attention my concerns with the handling of the barley deficiency payments which is part of the wheat and feed grains program enacted by the Food Security Act of 1985. There are serious problems with the way in which this program is currently being administered by the USDA. The problem is with the calculation of barley deficiency payments.

The Food Security Act of 1985 and subsequent USDA regulations stated that barley target prices, hence barley deficiency payments, would be set at a "fair and reasonable" relationship to the congressionally mandated corn target price. USDA regulations established barley target prices based upon bushel weight comparisons to corn. These regulations did not take into consideration the true feed value of barley or the value of barley as a food source.

At the same time, the USDA, in calculating the national average market price used in determining whether the farmer will receive a barley deficiency payment, added the higher priced Malting barley into the equation. The result was that the barley target price was lower than corn by significant amounts and the national average price determined by USDA was significantly higher than the price received by most Feed barley farmers. This caused many farmers who received advanced deficiency payments in 1988 to receive notices from USDA which demanded repayment of deficiency payments with funds that the farmer did not receive from the market.

I believe that this is totally unfair and have introduced a bill, S. 1000,[19] which is designed to eliminate this inequity. I am seeking passage of legislation which would change the way the national all barley price is calculated. There are two ways to redress this inequity. The first way is to adjust the target price of barley for the 1988 and 1989 crop-year to adequately reflect the total value of barley and the cost of production, or we can eliminate Malting barley from the formula used to calculate the national all barley price. If the USDA were to include the contribution of Malt barley when it determines the barley target price, the equation would be equal as the USDA includes the Malting barley average price in determining the deficiency payment. If this were done, barley farmers would be asked to repay only $.08 per bushel instead of the $.304 per bushel they are currently being asked to repay.

The other way to fix this problem is to exclude the value of Malting barley from the equation used to calculate the deficiency payment. The result would be the same to the farmer.

The administration has opposed all efforts at reforming this program claiming that it would set a precedent which could be detrimental to the operation of other programs such as wheat. There are several classes of wheat which at times bring significantly different values when sold. I do not dispute this fact, but I would like to point out that the USDA did not leave out of the equation the values of these wheats when they calculated the all wheat target price. Thus, when they calculated the deficiency payment by using all prices in determining the national average wheat price, there was no inequity. This is not true in the current method of calculating the barley deficiency payment.

Mr. Chairman, I am not going to address today the issue that will be before the Senate Agriculture Committee in the coming months—how to set the barley target price in the next 5 years. I want to and will confine my comments only to the problem created in the 1988 and 1989 barley program, namely the need to remove the Malting barley price from the determination of the national all barley price. I urge you to move on this alone at this time and offer some assistance to those farmers who are being asked to pay back deficiency payments with dollars they never received from the market.

Thank you Mr. Chairman. I look forward to working with you on this and other issues in the future.

Senator BAUCUS. Our first witness is from the Agricultural Stabilization and Conservation Service of the Department of Agriculture. He is the Administrator. Is Keith here? OK. Great. Keith, why don't you come up and give your testimony. Go ahead.

STATEMENT OF KEITH BJERKE, ADMINISTRATOR, AGRICULTURAL STABILIZATION AND CONSERVATION SERVICE (ASCS), U.S. DEPARTMENT OF AGRICULTURE, WASHINGTON, DC

Mr. BJERKE. Thank you, Mr. Chairman. I am Keith Bjerke, the Administrator of ASCS, and I brought a couple of experts with me today, and with your indulgence if we get into technical areas that I cannot answer, I would like to call on them.

Senator BAUCUS. Sure, sure.

INTRODUCTION

Mr. BJERKE. I am pleased to testify today on the related subjects of barley deficiency payment rate formula and the repayment of unearned advanced deficiency payments.

I would first like to briefly review the general deficiency payment rate formula and unearned advanced deficiency payments before discussing legislation that has already affected the repayment or at least hopes to affect the repayment of these advances. I will conclude with discussion of several of these issues, and then take questions as appropriate.

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[19] S. 1000, to amend the Agricultural Act of 1949 to require the Secretary of Agriculture to exclude the malting barley price from the national weighted market price for barley in determining the payment rate used to calculate deficiency payments for the 1989 and 1990 crops of barley, and for other purposes. Some provisions included in S. 2830.

CURRENT LAW PRESCRIBES THE MANNER IN WHICH DEFICIENCY PAYMENTS ARE TO BE DETERMINED

Current law prescribes the manner in which deficiency payments are to be determined. The 5-month deficiency payment is based on the difference between the established "target" price and the higher of the average market price for the first 5 months of the marketing year or the basic price support loan rate determined for the crop. If the Secretary of Agriculture reduces the basic price support rate, additional compensation must be provided to producers to ensure that the producer receives the same total return as if the adjustment in the price support rate had not been made. These additional payments may be made if the average market price over the 12 months of the marketing year, the 12-month price, is less than the basic price support rate. These payments are commonly referred to as "Findley payments" and are made as soon as practicable after the end of the marketing year.

Advance payments equal to 40 to 50 percent of our precrop projected payment rate are made during or after the signup but before harvest. To the extent that amounts required to be paid on the basis of the deficiency payment rates and Findley payment rates are less than the advance payments, the difference must be refunded by the producer. Such was the case with respect to the 1988 crop of barley requiring that barley producers refund payments at the rate of 30.4 cents per bushel.

Section 107C(2)(G) of the Agricultural Act of 1949 provides that "any refund required . . . shall be due at the end of the marketing year for the crop with respect to which such payments were made." Repayment of unearned 1988 deficiency payments, however, has been delayed numerous times by legislative action.

The Disaster Assistance Act of 1988 (the 1988 Act) authorized making of disaster payments to producers of disaster-affected crops but provided that the production used for computing earned deficiency payments shall be reduced by the quantity for which disaster payment was made. The 1988 Act further provided that, if any portion of the advance deficiency payment made to producers for disaster-affected crops must be repaid, such repayment shall not be required prior to July 31, 1989, for that portion of the crop for which a disaster payment was made under the 1988 Act. The 1988 Act also provided that repayment would be forgiven with respect to the first 35 percent of a producer's loss of production for these commodities, and if they did not then qualify for the disaster.

Subsequently, the Dire Emergency Supplemental Appropriation Act of 1989, Public Law 101-45, enacted on June 30, 1989, amended the 1988 Act to prohibit collection of disaster-caused overpayments before December 31, 1989. The Disaster Assistance Act of 1989 later amended the 1988 Act to prohibit collection of unearned advance deficiencies before July 31, 1990. Finally, Public Law 101-220, signed by the President on December 12, 1989, provides that for the 1988 program crops, any unearned portion of the advance deficiency payment made to producers who qualified for assistance under either the 1988 Act or 1989 Act shall not be required before July 31, 1990.

Under the legislation passed by Congress and signed by the President, barley producers who qualified for disaster assistance on either their 1988 or 1989 barley crop are not required to repay unearned 1988 advance deficiency payments for barley before July 31, 1990. Hopefully, this additional time will allow them to meet their obligations for repayment in a timely manner. Those barley producers who did not suffer 1988 or 1989 drought losses have been repaying their unearned 1988 advance deficiency payments over the last several weeks along with corn and oat producers across the Nation.

For a variety of reasons, many have recommended that we take immediate action to delay any further repayment of unearned deficiency payments for barley. However, to further delay any of these barley refunds which have yet to be made would be unfair not only to the barley producers who met their obligations in a timely manner, but also to corn and oat producers.

WHAT IS ALL THIS MISUNDERSTANDING AND CONTROVERSY ABOUT?

So what is all this misunderstanding and controversy about?

ONE ELEMENT IS THE PAYMENT RATE FORMULA

One element of the payment rate formula is, of course, the target price and the manner in which the barley target price is set, and this is the source of some misunderstanding. The Department of Agriculture (USDA) does not calculate the barley target price based on the relative feed value of barley to corn as many claim. Rather, USDA has maintained the target price of barley, despite its lower feed value in relation to corn, at a level equal to that of corn on a pound-for-pound basis for each corn crop-year covered by the Food Security Act of 1985. Had the barley target price been based on relative feed value, the barley target price would have been 95 percent of what it had been in each of those years.

In most years, the difference between the Feed barley and Malting barley prices is usually lower than it was in 1988, and setting the target price of barley at a level higher than its feed value in relation to corn has covered this spread in Malting barley versus Feed barley prices. The price spread between these two types of barley obviously widened with the droughts of 1988 and 1989 when Malting barley sold at a premium, so the average market price of "all" barley rose above the target price. If, as we all hope, producers experience more normal weather in 1990 and beyond, the price spread between Feed barley and Malting barley should narrow, and we should not experience this same problem into the future.

AVERAGE MARKET PRICE HAS BEEN THE SOURCE OF SOME CONTROVERSY AS IN THE CASE OF BARLEY

Another component of the payment rate formula, the average market price, has been the source of some controversy as in the case of barley.

Suggestions have been made that our determination of the payment rate is "unfair" because Malting barley prices have been added to the average market price calculation of "all" barley. It is true that the Malting barley price is part of the average market price of "all" barley. Moreover, the all-barley price is used in determining the deficiency payment rate for barley. However, this is not a new procedure. In each year that barley has been included in the Feed Grain Program going back to 1974, Malting barley prices have been used in the average market price determination and Malting barley producers have been allowed to be in the Feed Grain Program.

I might add that the use of average market prices is a problem that is inherent in determining deficiency payments for all program crops. When a segment of a market receives a higher price, the average price rises and the payment rate falls. In a given year, producers who receive a market price that is lower than the average do not get a bigger deficiency payment, while those who receive a higher-than-average price do not get a smaller deficiency payment. This aspect of the program is not peculiar to barley. For example, higher priced Acala cotton, high-protein Durum wheat, and long-grain rice are included in calculating the average market prices and, hence, deficiency payment rates for Upland cotton, "all" wheat and "all" rice, respectively.

Changing the payment rate for barley, so that those who sold their barley as feed would be paid a different rate from those who sold their barley for malt production, could well lead to calls for similar treatment by other commodity groups. USDA's position is that the programs for feed grains, wheat, rice, and cotton should remain national programs.

It may come as no surprise, then, that others argue that Malting barley should be excluded from the Feed Grain Program, advancing at least two arguments to support this contention. One is that the program is for feed grains and should therefore exclude grain used for nonfeed purposes. The other is that Malting barley commands a high price premium relative to Feed barley so Malting barley does not need price and income protection.

SEVERAL POINTS ARE IN ORDER

Several points are in order. First, it is not generally true that Malting barley commands a higher premium price relative to Feed barley. The 1988 crop's 12-month price of Malting barley used in the production of malt was $3.28 per bushel, a dollar higher than the corresponding Feed barley price. However, the price spread between the two uses of barley is typically much lower. For instance, the simple average of the annual price spreads for the 1982 through 1987 barley crops, leaving out 1988 and 1989, was only 20 cents a bushel.

Second, it is also not generally true that those who plant Malting barley necessarily harvest barley that is sold and subsequently used to produce malt. In 1988, for instance, the drought not only affected Malting barley yields but also the protein content of a sizable portion of the Malting barley crop, making it unacceptable to the brewing industry.

As a consequence, these producers had to sell their barley for feed at Feed barley prices. In normal years, moreover, there is generally more Malting barley planted and harvested than the brewing industry needs. Thus, it is not uncommon for Malting barley producers to only get a Feed barley price for their barley even though it has the desirable protein content and was grown for the malt market.

The fact that Malting barley as planted is often sold as Feed barley after harvest points out the difficulty in changing our barley payment rate calculation by using separate feed and Malting barley payment rates, as some have suggested. You only need to ask a few key questions to see that such a program is an administrative nightmare because of the verification problems, the various prices and levels in each of these categories.

For instance, how would we determine advance payment rates for participating producers? Even if advances for barley were eliminated, how would we determine 5-month and Findley payment rates for each producer? If we require receipts showing whether a producer sold barley as feed or malt, what do we do if the producer has not sold it at the 5-month point—does he get the lower payment rate? What if a producer does not sell at all and instead uses the barley for onfarm feed use or stores it—which rate do we pay him? What is to stop a producer who was paid a Malting barley price from saying he used his barley for onfarm feed use to simply get what could be a higher Feed barley payment rate?

SEPARATE PAYMENT RATES ARE TROUBLESOME IN OTHER WAYS

Aside from these issues, separate payment rates are troublesome in other ways. For instance, separate rates may still not avoid the problem of unearned advances, particularly for Malting barley producers. Moreover, anything that would increase the payment rate for a majority of producers would assuredly raise Federal outlays, perhaps substantially. Also, the separate rate approach for barley sets a precedent for other commodities, such as wheat, characterized by low- and high-valued uses.

Another suggested method of changing our payment rate calculation is to use the Feed barley price rather than the all barley price to determine the rate for all barley producers. Again, this would undoubtedly raise Federal outlays because the Feed barley price has traditionally been below the all barley price. As with the separate rate approach, adopting such an approach would set a precedent for other commodities. Finally, the Feed-barley-price-only approach would give a windfall to those Malting barley producers who may have received a premium price for their product already.

That concludes my testimony, Mr. Chairman, and I would be happy to respond to your questions.

Senator BAUCUS. Thank you, Mr. Administrator.

I notice we are joined by Senator Boschwitz. Senator, do you have a statement or comment you would like to make at this point?

Senator BOSCHWITZ. No. You know that Senator Conrad and I have been active in seeking some delays in the repayment of the advance deficiency payment and we have been troubled by some of the things that Administrator Bjerke has pointed out. I am aware that over the years that this issue has not really been raised, and as you pointed out since 1974——

Mr. BJERKE. Right.

Senator BOSCHWITZ [continuing]. The figuring of the deficiency payment has been on this all-barley approach and that some inequities have developed because of the drought when Malting barley became much more expensive. Are you a barley producer as well?

Mr. BJERKE. Yes, sir, I was before I had to leave the farm and join all of you here.

Senator BOSCHWITZ. I gather that a barley producer does not know in advance if his barley is going to be high protein or low protein, and so that you do not know if you are going to get Malting barley or Feed barley. Is that a fair statement?

Mr. BJERKE. That is true. In our part of the country where we try to grow Malting barley. There are some areas, of course, of the Nation that specifically plant Feed barley and know going in that it will be a Feed barley harvest.

Senator BOSCHWITZ. I gather that is the same in my State.

Mr. BJERKE. Yes, sir.

Senator BOSCHWITZ. The president of my State's barley association is going to be here. Your statement was quite clear, despite the numerous references to all of the changes that we have done legislatively, and sometimes you get lost in the fact that we extended the 6 months and then did it another time. I have to go back and read the agreement that Senator Conrad and I entered into with Senator Lugar the last time around. We may have agreed to not request a forgiveness at this point by getting the additional delay. Do you recall exactly the wording?

Mr. BJERKE. No, sir, I have not seen the statement. I have heard about it, but I have not seen the document.

Senator BOSCHWITZ. I will have to go back and review it. I am anxious to hear the barley producers' side of the story, Mr. Chairman. I thought that Mr. Bjerke's statement was clear and to the point and made comparisons to other crops. I might say that the calculation of the deficiency payments and the loans are somewhat different for cotton and rice than they are for feed grains. In the bill that I have introduced, I have made them all the same so that one set of crops are not advantaged either in the loans or in the calculation of deficiency payments. But I thank you for your testimony and I have no further questions.

Senator BAUCUS. Thank you, Senator. Mr. Administrator, Senator Boschwitz is correct. Your statement made your position clear. Your position, however, is certainly not the position of a lot of barley producers, at least in my part of the country. Your testimony pointed out two major objections to various solutions that have been offered. One objection is just complexity from the USDA's point of view, and the second is outlays. I frankly do not think that either of those are legitimate objections. It just seems to me that it is our job to find a solution regardless of the complexity. We are here to serve our people. We are not here to throw up objections as to why we cannot serve them. It is our job to serve them.

It is your job. It is my job. It is Senator Boschwitz' job. It is really not proper for us to, except in very extreme cases, come up with the excuse of complexity. We are here to try to find some equity for people, and I introduced legislation which I think is a solution. I very strongly urge the administration to go the extra mile to try to find some way we can solve some of these inequities because they do occur.

Mr. **Bjerke**. That is right.

Senator **Baucus**. And we in Montana do not have a lot of flexibility with the crops we can grow. We cannot grow lots of different kinds of crops that some other folks can grow. We have a special situation there, and it is more risky for us in our part of the country than in other parts of the country. And so I just strongly urge you to work with this committee and the Congress in trying to find a solution here.

In addition, when it comes to outlays it seems again that we have to find a solution that is fair to people.

The administration has not been forthcoming, and I know you have your marching orders from different parts of the administration, and I understand that. I am not going to quarrel with you particularly over that, but we intend to find a solution here because people have been hurt, and we have to provide a solution. Thank you. I have no further questions.

Mr. **Bjerke**. Thank you.

Senator **Baucus**. Thank you.

Our panel now includes George Paul, executive director of Montana Farmers Union; Marsha Jones, who is the National Grains Chairperson of Women Involved in Farm Economics (WIFE); Mr. Stephen Naught, who is vice president of the National Barley Growers Association; Mr. Tim McGreevy, administrator of the Idaho Barley Commission; and Gerald Lacey, president of the Minnesota Barley Growers Association.

Senator **Boschwitz**. Mr. Chairman I understand that you may want to listen to Mr. Paul's testimony first. I wonder if we could go on to Mr. Lacey because I am afraid I have a schedule of appointments this afternoon, and I would like to hear the witness from your State as well as the president of Minnesota Barley Growers Association.

Senator **Baucus**. Yes. Who do you want first?

Senator **Boschwitz**. Please go with Mr. Paul.

Senator **Baucus**. George, you are first, yes. Then we will do Mr. Lacey second.

Senator **Boschwitz**. Yes.

STATEMENT OF GEORGE V. PAUL, EXECUTIVE DIRECTOR, MONTANA FARMERS UNION, GREAT FALLS, MT

INTRODUCTION

Mr. **Paul**. Thank you. Good afternoon. For the record, my name is George Paul.

I am executive director of Montana Farmers Union, a general farm organization representing over 3,500 agricultural producers. I am speaking in that capacity today.

I want to acknowledge the cooperation and support of the National Farmers Union, National Barley Growers Association, the Montana Grain Growers Association, and the Fairfield Bench area producers. We have worked together to develop testimony which we hope is meaningful to you and accurately represents the interests of Montana Feed and Malt barley producers.

Senator **Boschwitz**. What is the Fairfield Bench? It sounds like you have a bunch of lawyers here.

Senator **Baucus**. Oh, no, far from it.

Mr. **Paul**. 85,000 acres of irrigated barley ground.

Senator **Baucus**. That is right. That is irrigated.

Senator **Boschwitz**. Oh, it is called——

Senator **Baucus**. It is northwest of Great Falls, Montana.

Mr. **Paul**. It is the barley capital of the world, I will have you know, sir.

Senator **Boschwitz**. Hold on. [Laughter.]

Mr. **Paul**. In certain instances.

Senator **Boschwitz**. Oh.

Senator **Baucus**. You asked. [Laughter.]

Senator **Boschwitz**. It is just an area, and it is called the Fairfield Bench.

Mr. **Paul**. It is. The Fairfield Bench.

Montana Farmers Union also wants to thank you, Senator Baucus, for your interest and efforts in helping solve the crisis which faces our barley producers today. That crisis was, in part, created by your colleagues 2 years ago in this very room. I will expand on that in a moment. Do not get excited, Senator Boschwitz.

Senator **Boschwitz**. I was here, and he was not. [Laughter.]

FIRST, I WANT TO FOCUS ON THE BARLEY INDUSTRY AND ITS IMPORTANCE IN THE MOSAIC OF AMERICAN AGRICULTURE

Mr. **Paul**. First, I want to focus on the barley industry and its importance in the mosaic of American agriculture.

Too long, barley has been treated as a minor player, as some tag-along crop. Traditionally, it has been cast in the part of the not-so-welcome stepchild to corn or as the distant relative by wheat interests. Feed barley was what you bought if you could not get corn, or what you grew if you were not planting wheat. An alternate crop, an alternate commodity.

BARLEY HAS MATURED

Well, that was then and this is now. Barley has matured. As a food commodity, barley is not just for beer anymore. And it has grown way beyond barley soup. For years, barley has been used as a substantial food item in certain foreign countries. Taiwan is the leader in this regard, and the interest in Japan is growing at a very fast rate. In the United States, research regarding the performance of barley as a cholesterol stripper is being recognized by nutritionists and food processors. Consumer interest and demand are on the rise.

As a feed product, barley has established its proper place in the market. Corn is king, always has been, probably always will be. That is just fine. But barley is a prince in its own right and should be recognized and treated with no less regard.

Senator **Boschwitz**. This guy is a poet.

Senator BAUCUS. Yes.

Mr. PAUL. Barley has——

Senator BOSCHWITZ. Fairfield Bench.

Mr. PAUL. That is right.

Senator BOSCHWITZ. You do not often hear that in this committee.

BARLEY HAS A MAJOR FINANCIAL IMPACT IN THE NORTHERN TIER STATES WHERE IT IS GROWN

Mr. PAUL. Barley has a major financial impact in the northern tier States where it is grown. In Montana, barley normally is planted to some 2 million acres and averages well over $100 million in annual farm receipts. Of the total barley crop each year in Montana, about 85 percent is barley for Feed, while 15 percent is barley for Malt.

Contrary to a statement made by Secretary Yeutter in his February 20, 1990, letter to you and 19 of your colleagues, and frankly the statement just earlier made by Mr. Bjerke, there is a substantial difference between Feed barley and Malting barley prices in normal years. "The Five-Year Average of Barley Prices 1984 through 1989," figures compiled by the U.S. Department of Agriculture, shows a 39 cent per bushel Malting premium over Feed.

In Montana, the barley producers consider 39 cents is a substantial difference on a commodity that averages $2.10 a bushel.

COMMODITY PRICING AND DEFICIENCY PAYMENT FORMULAS

Commodity pricing and deficiency payment formulas are the subject of other testimony here today, and while we are supportive of much of that testimony, Montana Farmers Union chooses to focus on this dilemma from a slightly different angle.

I stated earlier that the barley advance deficiency payment payback crisis is one created partially by your colleagues. That crisis creation took place here in this room during the summer of 1988. Let me emphasize the crisis was not by design, but rather by the desire to help a ravaged industry, and the inability to outguess the weather.

RECALL THE SITUATION

Let us recall the situation at its beginning. Disastrous weather was holding firm in its grasp a nation of producers. No one was imagining worse weather. The weather damaged crops came at a time of low commodity prices, which were designed as part of the Food Security Act of 1985, to help clear the "glut of grain" which many believed was plaguing the marketplace.

Producers were now contending with low commodity prices and unavoidable crop failure. Members of Congress responded with the Disaster Assistance Act of 1988.

They were determined to not be idle while Mother Nature drove the last nail in the coffin of an already beleaguered agriculture industry.

Their concern at the time was to leave as much money as possible in the hands of the producers. They recognized that not only producers needed assistance but also the rural communities those producers support. They knew that providing moneys at the producer level, both the farmer and the local community would benefit.

Discussions held during those bill creating sessions eventually led to the subject of barley advance deficiency payback. The loss of the crop had sent barley prices rising beyond the target price level and triggered the prescribed payback.

Producers who had used those advance payments to plant a now-failed crop were required to pay back the Government. In theory at least, they would use moneys collected from the marketplace, received from higher prices generated by some market force. Unfortunately for all, the market force in this case was a crop disaster, meaning even though prices were favorable, there were no bushels to sell at any price.

The Senate recognized the dilemma and realized it made little sense to send out a disaster fund check to a producer while he was mailing in a deficiency payment check to the Government. To avoid checks "crossing in the mail," as it were, a 1-year moratorium for deficiency paybacks became a part of the Disaster Act. Producers would have use of the funds to plant another crop. The next expenditures for the disaster legislation would be reduced, and the debt would be paid back in July of 1989 after a good crop had been marketed.

Then the unimaginable happened. A second year of drought. There was no crop in 1989.

The repeated scenario appropriately brought a repeated action from Congress. I realize nobody here at the table, certainly you two Senators, need the history lesson, but we feel this refresher is important just to make this point easy to follow now.

Our contention is that at the time of the first moratorium, it was the intent of Congress to leave as much money as possible in the hands of the producer to mitigate the effects of the disaster. Therefore, even though the dollars came from a deficiency payment fund, they were clearly being treated by Congress as disaster moneys at the time of the moratorium.

Disaster payments are not paid back. Why then should a producer be asked to repay these converted disaster dollars? We would ask that members review this situation and support legislation to permanently delay the advance deficiency, the advance barley deficiency payments made to producers who qualified for assistance under that disaster legislation.

TWO FINAL POINTS

Two final points, sir. One, we believe the Secretary has the administrative authority to grant this request. He has refused to do so, and we have no reason to think at this time that he will act in favor of the producer in this matter. Congress is the producer's hope to correct this situation.

Two, the calculation formulas have been flawed for years. You are going to hear that in other testimony presented here today. At the very least, applying a corrected formula to this situation would go a long way toward making things right. And that is all we are asking for, is just to make it right.

We appreciate that "agricultural forgiveness" is not easy to sell inside the beltway, especially to an urban Congress. To say this may not be politically palatable is an understatement. But, we believe our position to be right, considering the intent of Congress at the time.

We ask that you provide the leadership and honesty with this issue as you have always done for us in the past. On behalf of the barley producers in Montana and Montana Farmers Union, we thank you for this opportunity to be heard. Thank you, sir.

Senator BAUCUS. Thank you very much, George.

[The prepared statement of Mr. Paul follows:]

A Hearing
on
Barley Advance Deficiency Payments

Before the
Subcommittee on
Agricultural Production and Stabilization of Prices
of the
Committee on
Agriculture, Nutrition and Forestry

Honorable
Senator Max Baucus
Presiding

Testimony of
George V. Paul
Executive Director
Montana Farmers Union

April 19, 1990
2:00 p.m.
328A Senate Russell Building

FARMERS UNION

Good afternoon. For the record, my name is George Paul.

I have been involved with the barley and wheat industry for thirteen years. I have served with the Montana Department of Agriculture Director's Office as Administrative Assistant, the Montana Wheat and Barley Committee as Information Officer and Market Analyst, and the United States Senate Committee on Agriculture, Nutrition and Forestry as Professional Staff Member on the Subcommittee on Agricultural Production and Stabilization of Prices.

Currently, I am Executive Director of Montana Farmers Union, a general farm organization representing over 3,500 agricultural producers. I am speaking in that capacity today.

I want to acknowledge the cooperation and support of the National Farmers Union, the National Barley Growers Association, the Montana Grain Growers Association, and the Fairfield Bench area producers. We have worked together to develop testimony which we hope is meaningful to you and accurately represents the interests of Montana feed and malt barley producers.

Montana Farmers Union also wants to thank you, Senator Baucus, for your interest and efforts in helping solve the crisis which faces our barley producers today. That crisis was, in part, created by your colleagues two years ago in this very room. I'll expand on that in a moment. First, I want to take a minute to focus on the barley industry and its importance in the mosaic of American agriculture.

Too long, barley has been treated as a minor player, as some tag-a-long crop. Traditionally, it has been cast in the part of the not-so-welcome stepchild to corn or as the distant relative by wheat interests. Feed barley was what you bought if you couldn't get corn or what you grew if you weren't planting wheat. An alternate crop, an alternate commodity.

Well, that was then and this is now. Barley has matured. As a food commodity, barley isn't just for beer anymore. And it has grown way beyond barley soup. For years, barley has been used as a substantial food item in certain foreign countries. Taiwan is the leader in this regard, and the interest in Japan is growing at a fast rate. In the United States, research regarding the performance of barley as a cholesterol stripper is being recognized by nutritionists and food processors. Consumer interest and demand are on the rise.

As a feed product, barley has established its proper place in the market. Corn is king, always has been and always will be. That's just fine. But barley is a prince in its own right and should be recognized and treated with no less regard.

Barley has a major financial impact in the Northern Tier states where it is grown. In Montana, barley normally is planted to some two million acres and averages well over $100 million in annual farm receipts. Of the total barley crop each year, about 85 percent is barley for feed, while 15 percent is barley for malt.

Contrary to a statement made by Secretary Yeutter in his February 20, 1990, letter to you and nineteen of your colleagues, there is a substantial difference between feed barley and malting barley prices in normal years. "The Five-Year Average of Barley Prices 1984 through 1989", compiled by USDA, shows a $0.39 per bushel malting premium over feed.

Montana barley producers consider 39 cents to be substantial on a commodity averaging $2.10 per bushel. We disagree with the secretary's letter writer that "the difference between feed-barley and malting-barley prices is small."

Commodity pricing and deficiency payment formulas are the subject of other testimony here today, and while we are supportive of much of that testimony, Montana Farmers Union chooses to focus on this dilemma from a slightly different angle.

I stated earlier that the barley advance deficiency payment payback crisis is one created partially by your colleagues. That crisis creation took place in this room during the summer of 1988. Let me emphasize the crisis was not by design, but rather by desire to help a ravaged industry, and the inability to outguess the weather.

Let's recall for a minute the situation at its beginning. Disastrous weather was holding firm in its grasp a nation of producers who had made America the world's food store. No one was imagining worse weather. The weather damaged crops came at a time of low commodity prices, designed as part of the 1985 Food Security Act, to help clear the "glut of grain" which many believed was plaguing the marketplace.

Producers were now contending with low commodity prices and unavoidable crop failure. Members of Congress responded with the Disaster Assistance Act of 1988.

They were determined to not be idle while Mother Nature drove the last nail in the coffin of an already-beleaguered agriculture industry--the industry which was providing nearly 20 percent of the jobs in this nation and was the only bright spot in an otherwise dreary export agenda.

Their concern at the time was to leave as much money as possible in the hands of the producers. They recognized that not only producers needed assistance but also the rural communities those producers supported. They knew that by providing monies at the producer level, both the farmer and the local community would benefit.

Discussions held during those bill-creating sessions eventually led to the subject of barley advance deficiency payback. The loss of the crop had sent barley prices rising beyond the target price level and triggering the prescribed payback.

Producers who had used those advance payments to plant a now-failed crop were required to pay back the government. In theory at least, they would use monies collected from the marketplace, received from higher prices generated by some market force. Unfortunately for all, the market force in this case was a crop disaster, meaning even though prices were favorable, there were no bushels to sell at any prices.

The Senate recognized the dilemma and realized it made little sense to send out a disaster fund check to a producer while he was mailing in a deficiency payment check. To avoid checks "crossing in the mail," as it were, a one-year moratorium for deficiency paybacks became a part of the Disaster Act. Producers would have use of the funds to plant another crop; new expenditures for the disaster would be reduced, and the debt would be paid back in July 1989, after a good crop had been marketed.

Then the unimaginable happened. Someone forgot to tell Mother Nature there would be no bad weather in '89. A second year of drought developed on the heels of the '88 disaster. There was no crop in '89.

The repeated scenario appropriately brought a repeated action from Congress. The disaster legislation written in '89 would again carry a moratorium for the payments; this time until December of '89. Ultimately, no payments would be collected before early 1990. I realize none here needs the history lesson, but the refresher will make it easier to follow the point.

Our contention is that at the time of the first moratorium, it was the intent of Congress to leave as much money as possible in the hands of the producer to mitigate the disaster. Therefore, even though the dollars came from a deficiency payment fund, they were clearly being treated as disaster monies at the time of the moratorium.

Disaster payments are not paid back. Why then, should a producer be asked to repay these converted disaster dollars? We would ask that members review this situation and support legislation which would permanently delay or forgive the advance barley deficiency payments made to producers who qualified for assistance under the disaster legislation of 1988 or 1989.

Two final points. One, we believe the secretary has administrative authority to grant this request. He has refused to do so, and we have no reason to think he will act in favor of the producer in this matter. Congress is the producers' hope to correct this situation.

Two, the calculation formulas have been flawed for years as is presented in other testimony today. At the very least, applying a corrected formula to this situation would go a long way towards making things right. And that is all we are asking for.

We appreciate that "agricultural forgiveness" is not easy to sell inside the Beltway, especially to an urban Congress that doesn't fully understand the issue. To say this may not be politically palatable is an understatement. But, we believe our position to be right, considering the intent of Congress at the time.

We ask that you provide the leadership and honesty with this issue as you have always done for us in the past. On behalf of our barley producers, Montana Farmers Union thanks you for the opportunity to be heard.

Senator BAUCUS. Mr. Lacey.

Senator BOSCHWITZ. I would say for the record, Mr. Chairman, that Mr. Lacey is the president of the Minnesota Barley Growers Association. He is a barley grower from Campbell, Minnesota, and I am not sure that I have ever been in Campbell. But I have been in most of the whistlestops. Perhaps I should not call it that. Tom Dewey got into a little trouble in 1948 when he accused President Truman of—was it Dewey—of stopping at every whistlestop.

Senator BAUCUS. It was Dewey. It had to have been Dewey.

Senator BOSCHWITZ. Campbell, I think, would be fairly——

Mr. LACEY. It is a whistlestop.

Senator BOSCHWITZ. It is a whistlestop, yes.

Mr. LACEY. But you have been in our county seat, Elbow Lake.

Senator BOSCHWITZ. Oh, Elbow Lake, right by Elbow Lake.

Mr. LACEY. Yes.

Senator BOSCHWITZ. I see. That is a very pretty part of the State. Thank you very much.

STATEMENT OF GERALD A. LACEY, PRESIDENT, MINNESOTA BARLEY GROWERS ASSOCIATION, CAMPBELL, MN

INTRODUCTION

Mr. LACEY. Mr. Chairman and Senator Boschwitz, I am Gerald Lacey, a barley grower from Campbell, Minnesota. I am president of the newly formed Minnesota Barley Growers Association and a director of the National Barley Growers Association. I appear before you today as a representative of midwestern barley growers to discuss two primary issues which are devastating growers throughout the United States, namely the repayment of the advanced barley deficiency payment received in crop-years 1988 and 1989, and the potential treatment of barley growers in the upcoming 1990 Food Security Act.

I WOULD LIKE TO DISCUSS THE BARLEY DEFICIENCY REPAYMENT ISSUE

First, I would like to discuss the barley deficiency repayment issue. The current dilemma reverts back to the Agriculture and Food Act of 1981. Prior to the 1981 act, target prices for the program crops were a function of the cost of production. The 1981 act, however, mandated specific target price minimums for corn throughout the life of the bill. It also specified that the target price levels for barley, sorghum, and oats were to be set at a "fair and reasonable level" in relation to corn. The Food Security Act of 1985 followed a similar tack. This system severely biases the target prices for barley due to the differing relationships between the cost of production and the yields of barley and corn.

EXAMPLES OF HOW BARLEY HAS BEEN IMPACTED BY THE PAST TWO FARM BILLS

Let me cite a couple of examples of how barley has been impacted by the past two farm bills. In 1981, prior to the influence of the 1981 and 1985 bills, target prices for barley and corn were at about 80 percent of their respective cost of production. Subsequent farm bill legislation has changed those relationships over time to a point today where the barley target price is only 73 percent of the cost of production, while corn is currently at approximately 112 percent. The relationship between the sorghum target price and the cost of production is similar to that of corn.

The devastating effects of this situation can be seen in the current versus historic acreage. Planted barley acreage is expected to be below 9 million acres this year, down over 30 percent from where we were just 5 short years ago. This is a direct effect of the inequities within the previous farm bill legislation. If something is not done immediately to rectify this situation, barley may cease to exist to be a viable industry in the United States and may become a net-importing country as it is in the case with oats.

DROUGHTS OF 1988 AND 1989

The droughts of 1988 and 1989, along with the drought potential in 1990, have magnified the inequities within the current program. The majority of the Malting barley is produced in the Midwest. However, Malting barley has never been included, either directly or indirectly, as a component in setting the target price of barley. Yet, Malting barley is included in the determination of deficiency payments. We view this as a gross inequity which bears your consideration.

In the 1987 season, it was as about as typical as it gets in Minnesota as far as production and as far as the price were concerned. Malting barley growers averaged somewhere around from $150 to $180 per acre in gross returns, including deficiency payments and assuming average U.S. Malting barley prices.

The situation changed and developed into a critical state for the barley producers in 1988 when the average grower returned only about $93 per acre. That is the average grower. Less than one-half of our barley made Malting rate and subsequently it was sold for Feed barley prices which were about $1 per bushel below Malting barley prices. While the disaster assistance program was certainly a help, it only accounts for perhaps another $5 per acre return for the average Minnesota grower. What all this means is that between 1987 and 1988, our gross returns per acre fell by $60 per acre. Even if the entire advance deficiency is forgiven on barley, it would only amount to another $15 per acre for the average grower and the result is a $45 per acre shortfall compared to the 1987 and the normal. A potentially similar situation exists for the upcoming 1990 year.

SENATE BILL 1000

We believe that Senate bill 1000 introduced by Senator McClure, is on the right track perhaps toward rectifying the inequity of the barley deficiency repayment. Senate bill 1000 simply removes the Malting barley price from the average price used by the USDA to determine deficiency payments. However, we strongly suggest that this bill be amended to include the crop-year of 1988 in the recalculation of deficiency payments. After all, it was in that year that the greatest inequities with the current farm bill legislation surfaced. Growers would still be required to repay about 8 cents per bushel of the $.304 per bushel advanced, about the same as the corn growers are required to repay.

ONE COMMON MISCONCEPTION

One common misconception is that Malting barley growers who entered the farm program will obtain windfall profits if included in the deficiency repayment calculations. That is not the case. We must be cognizant that Malting barley yields are often lower, input costs are higher, management practices more intensive, and market returns more uncertain than with Feed barley grown in the Midwest. In addition, little of the Malting barley acreage in the Midwest is grown under contract and subsequently, quality requirements and quality acceptance is out of the producers' hands and is subject to the whims of the marketplace and the weather.

SECOND MAJOR ISSUE IS TREATMENT OF BARLEY GROWERS WITHIN THE 1990 FOOD SECURITY ACT

The second major issue is treatment of barley growers within the 1990 Food Security Act. We certainly appreciate the position Congress is in with regard to the Federal deficit and the budget reduction measures which will be required to bring the deficit under control. But we as barley growers appeal to your sense of fairness to bring the barley back in line with the other program commodities. We have endured 10 years of inequity within farm programs and feel it is only just that the target price of barley be realigned to bring us up to the levels with other farm program commodities. We do not, however, advocate the reduction in target prices of other program commodities.

As I stated previously, the target price for barley is only about 73 percent of the cost of production, while other commodities, with the exception of oats, are near or exceed their cost of production.

Mr. Chairman, Senator Boschwitz, and the rest of the committee, I appreciate the opportunity to appear before you today and I will be happy to answer any questions you have.

Senator BAUCUS. Thank you very much, Mr. Lacey.

[The prepared statement of Mr. Lacey follows:]

STATEMENT OF

GERALD A. LACEY
PRESIDENT
MINNESOTA BARLEY GROWERS
ASSOCIATION

BEFORE THE
SUBCOMMITTEE ON AGRICULTURAL PRODUCTION
&
STABLIZATION OF PRICES
UNITED STATES SENATE

REGARDING

1988 AND 1989 BARLEY DEFICIENCY REPAYMENT
&
BARLEY POSITION IN 1990 FARM PROGRAM

THURSDAY, APRIL 19, 1990

Mr. Chairman, members of the Committee, I am Gerald Lacey, a barley grower from Campbell, Minnesota. I am President of the Minnesota Barley Growers Association and a Director of the National Barley Growers Association. I appear before you today as a representative of midwestern barley growers to discuss two primary issues which are devastating growers throughout the United States, namely repayment of the advanced barley deficiency payment received in crop years 1988 and 1989, and the potential treatment of barley growers in the upcoming 1990 Food Security Act.

First, I would like to discuss the barley deficiency repayment issue. The current dilemma reverts back to the Agriculture and Food Act of 1981. Prior to the 1981 Act target prices for program crops were a function of the cost of production The 1981 Act, however, mandated specific target price minimums for corn throughout the life of the bill. It also specified that target price levels for barley, sorghum, and oats were to be set at a "fair and reasonable level" in relation to corn. The 1985 Food Security Act followed a similar tack. This system severly biases target prices for barley due to differing relationships between cost of production and yields of barley and corn.

Let me cite you a couple of examples of how barley has been impacted by the past two farm bills. In 1981, prior to the influence of the 1981 and 1985 bills, target prices for barley and corn were at about 80 percent of their respective cost of production. Subsequent farm bill legislation has changed those relationships over time to a point today where the barley target price is only 73 percent the cost of production, while corn currently is at approximately 112 percent. The relationship between the sorghum target price and cost production is similar to that of corn.

The devastating effects of this situation can be seen in current versus historic acreage. Planted barley acreage is expected to be below 9 million acres this year, down over 30 percent from where we were just five short years ago. This is a direct effect of the inequities within previous farm bill legislation. If something isn't done immediately to rectify this situation, barley may cease to exist as a viable industry within the U.S. and we may become a net-importing country as is the case with oats.

The droughts of 1988 and 1989, along with the drought potential in 1990 have magnified the inequities within the current program. The majority of malting barley is produced in the midwest. However, malting barley has never been included, either directly or indirectly, as a component in setting the target price of barley. Yet, malting barley is included in the determination of deficiency payments. We view this as a gross inequity which bears your consideraton.

The 1987 season was fairly typical in Minnesota as far as production and price were concerned. Malting barley growers averaged somewhere around $150 to $180 per acre in gross returns, including deficiency payments and assuming average U.S. malting barley prices.

The situation changed and developed into a critical state for barley producers in 1988 when the average grower returned only about $93 per acre. Less than one-half of our barley made malting grade and, consequently was sold at feed barley prices which were about one dollar per bushel below malting barley prices. While the disaster assistance program was certainly of help, it only accounts for perhaps another $5 per acre return to the average Minnesota grower. What all this means is that between 1987 and 1988, our gross returns per acre fell by $60 per acre. Even if the entire advance deficiency is forgiven on barley, it would only amount to another $15 per acre for the average grower and result in a $45 per acre shortfall compared to 1987 and the normal. A potentially similar situation exists for 1990.

We believe SB 1000, introduced by Senator McClure, is on the right track towards rectifying the inequity of the barley deficiency repayment. SB 1000 simply removes the malting barley price from the average price used by USDA to determine deficiency payments. However, we strongly suggest that SB 1000 amended to include crop year 1988 in the recalculation of deficiency repayments. After all, it was in that year that the greatest inequities with current farm bill legislation surfaced. Growers would still be required to repay about $.08 per bushel of the $.304 per bushel advanced, about the same as corn growers are required to repay.

One common misconception is that malting barley growers who entered the farm program will obtain windfall profits if included in the deficiency repayment calculations. That is not the case. We must be cognizant that malting barley yields are often lower, input costs higher, management practices more intensive, and market returns more uncertain than with feed barley grown in the midwest. In addition, little of the malting barley acreage in the midwest is grown under contract and subsequently, quality requirements and quality acceptance is out of the producers hands and is subject to the whims of the market place.

The second major issue is treatment of barley growers within the 1990 Food Security Act. We certainly appreciate the position Congress is in with regard to the Federal deficit and the budget reduction measures which will be required to bring the deficit under control. But we as barley growers appeal to your sense of fairness to bring barley back in line with other program commodities. We have endured ten years of inequity within farm programs and feel it it only just that the target price of barley be realigned to bring us up to the levels of other program commodities. We do not, however, advocate reduction in target prices for other program commodities.

As I stated previously, the target price for barley is only about 73 percent the cost of production, while other commodities, with the execption of oats, are near or exceed their cost of production.

Mr. Chairman, members of the Committee, I appreciate the opportunity to appeal before you today and would happy to answer any questions you may have.

Senator Boschwitz. Mr. Chairman, is it possible that we might ask questions of the first two witnesses?

Senator Baucus. Fine. Go ahead. I know you have to leave so why don't you go ahead.

Senator Boschwitz. I would like to ask several questions of both witnesses. First, I noted that there are 9 million acres, and there are 2 million in Montana, I gather. How many acres in the State of Minnesota are in barley?

Mr. Lacey. How many in total now?

Senator Boschwitz. How many acres in Minnesota are in barley?

Mr. Lacey. I do not have acres.

Senator Boschwitz. Do you know?

Mr. Lacey. It would be about 1 million acres.

Senator Boschwitz. Pardon me?

Mr. Lacey. About 1 million acres. I can give you specific bushels.

Senator Boschwitz. I am pleased that you addressed the target price and the way it is constructed and the percentage of cost of production, and I note at the very end you do not advocate reduction in target prices for other program commodities. It may be difficult to raise yours and stay within budgetary constraints and not make some adjustments elsewhere. The adjustments do not necessarily have to be made in target prices or deficiency payments. Perhaps some savings can be found in other elements of the farm bill. I will look for them. But I would forewarn you that that may not be entirely possible.

You say we have endured 10 years of inequity. I do not recall that the barley growers have been out in force stating that inequity until now when we had this drought and the corresponding increases in prices of the Malting barley. But has that been brought to our attention before?

Mr. Lacey. I do not think so, Senator. For one thing, Malting barley as a whole is only grown in about six, seven, eight States at the most, along the north side where we farm. And our organization is younger than we would like. You know, Senator, in Minnesota, we are just over a year old, and we have not had a unified voice. North Dakota, which is the major producing barley State, is the largest producing State. Our neighbor has only been organized for approximately 3 years. So the barley producers have not been able to speak as a good unified voice for some time. We are just getting our act together.

Senator Boschwitz. I see that we have 925,000 acres, about 1 million acres as you said.

Mr. Lacey. Yes.

Senator Boschwitz. My figures show about 10 million acres nationally. I note in your testimony that you say that Malting barley has never been included as a component in setting the target price and that it is a gross inequity. You said later on that the growing of Malting barley is more expensive than Feed barley; is that correct?

Mr. Lacey. Yes, it is. If we set out to grow Malting barley, we fertilize it differently. We treat it, we have to intend to grow less bushels per acre. Mother Nature has a lot to do with it, but we head for a lesser yield because we intentionally head for a protein that is lower. We fertilize it with less nitrogen, and we have to manage it, even plant it at a lesser rate.

Senator BOSCHWITZ. Could you elaborate a little further or review the reasons why farmers saw their gross returns fall by $60 an acre from 1987 to 1988?

Mr. LACEY. Yes, sir. That reduction in our—let us take my farm for an example—I raised 12 bushel that year in 1988. 12 bushel was my yield. So I can relate to that very closely.

Senator BOSCHWITZ. The average in your——

Mr. LACEY. Really there was no sale for it.

Senator BOSCHWITZ [continuing]. County is what—about 60?

Mr. LACEY. No, the county average is 49.

Senator BOSCHWITZ. Oh.

Mr. LACEY. But there is some proven yields in our county over 70. But the 12 bushels that I raised did not qualify for Malting. It would hardly qualify to be sold as Feed because it was barely able to be harvested. In fact, if I had not had a brother with a straight header, we could not have cut it and picked it up. It was that thin. So there was no quality there. So not only was the yield down, there was not any value to sell, and most of the farmers that are really hurting, the ones who have not had to pay back yet—thanks to you, Senator—those are the people that are really going to get hurt and hurt so badly that I do not know if they can survive.

There are some farmers out there that they do not know where they are going to find that money to pay back that deficiency that we included in the disaster. The bankers will not back them. There is a number of them that I really fear for their existence as farmers.

Senator BOSCHWITZ. Tell me about the prospects both in Montana and in Minnesota for a crop this year. Is your soil still pretty dry up there?

Mr. LACEY. Yes, sir. This is, I think—you know, sir, I farm a fair amount of acres and I came through the 1970's when things were good. And this is my first year at carrying crop insurance. Never felt that I could not carry my own insurance until this year. I do not feel I can this year. I have to have insurance, and I have to have the help because we do not have any excess moisture, and I cannot stand another one. My bankroll, my self-insurance bankroll is depleted.

Senator BOSCHWITZ. Mr. Paul is your area also dry? It is irrigated, I gather.

Mr. PAUL. The Fairfield Bench, yes. But, no, across Montana, eastern Montana, Senator, is still extremely dry, especially in our northeastern corner. And the breadbasket, if you will, which we call the golden triangle which includes the Fairfield Bench, we have had a reasonably good winter, but if we do not have timely spring rains, we could still have producers sitting there on a very negligible crop.

Senator BOSCHWITZ. If the 5-year average of barley prices from 1984 to 1989 showed a 39 cent per bushel Malting premium over Feed, why did you not complain about it at that time, may I ask?

Mr. PAUL. I guess what we are complaining about, Senator, is that we keep hearing——

Senator BOSCHWITZ. Why did you not bring it to our attention?

Mr. Paul. Yes, OK. Thank you. What we keep hearing from the U.S. Department of Agriculture is there is no significant difference between the Feed barley price and the Malt barley price, and in fact, there was a letter written to perhaps yourself and 19 of your colleagues, 20 of you got a letter from the Secretary on the 20th of February that stated that that difference is very small, and that simply is not the case. And what I am concerned about is if, especially at the staff level in USDA, if there are people there who really believe that, then there is a substantial difference in factual thinking between those people who are interpreting and running these programs and the producers that are out there growing the crop. It is a basic point that needs to be agreed upon somewhere in there so they can move forward with any of these programs or any type of program.

Senator Boschwitz. I would point out to my colleague from the State of Washington who came late that this gentleman represents all these folks including the Fairfield Bench, and I thought that we had a bunch of lawyers in here, but apparently it is an area of the State. Tell me——

Senator Gorton. The bench is the judges. The bar is the lawyers.

Senator Boschwitz. Well, the judges are normally lawyers too, though. But I better not get into that. But tell me—you are a very articulate fellow—what is the basic inequity? The wheat people and the corn people, corn had to repay, as was pointed out by Mr. Lacey, only 8 cents. But where is the basic inequity? Why should we act for barley? I have acted for barley, and so I have a sense of the answer. But where is the basic inequity that we should tell our colleagues that we have to do this for barley even though it is not being done for other crops?

Mr. Paul. I do not mean to sound philosophical in this, but as long as you asked. Senator Baucus, you know, hit on that earlier in speaking with Mr. Bjerke about complexity. Traditionally, you write national legislation. The Department tries to carry that out for everybody. Everybody gets hooked together. The fact is, Senator, that a lot of these commodities that do get hooked together and basically one is treated as a percentage of another and that kind of thing, these are separate and distinct commodities that cannot be linked together. But I think for convenience sake—and this is certainly not a ripping of the Department—but for convenience sake a lot of times they do get hooked together. And that is the wrong reason to let one feed off the other. Barley, and especially within barley, there is another whole level of problems they are going to have to deal with at some point.

So if complexity is the name of the game, they better gear up for it. Because right now we are only holding this discussion in terms of Feed barley and Malting barley, but what about Food barley uses? Is that going to muddy the waters even further somewhere down the road because barley as a food product is really gaining ground. You go into the research community, you hear a lot more about Food barley. Well, does that put in another layer of complexity that these people are going to have to deal with?

Senator Boschwitz. But yet, to make Mr. Bjerke's case for just a moment, there are many varieties of cotton, rice, and wheat.

Mr. Paul. Sure.

Senator BOSCHWITZ. And yet there has to be some averaging. You may be hardpressed to come to us on a 10 million acre crop, relatively small crop—I have to be careful about the words because I do not want to say poor cousin or anything—but how do we answer the argument that there should be special considerations for these subdivisions of a relatively small crop but not for cotton, rice, and wheat?

Mr. NAUGHT. Senator, may I address that question?

Senator BOSCHWITZ. Sure.

Senator BAUCUS. One or two. We have a lot of witnesses, and I know Senator Gorton has not had a chance to speak yet. I just wonder, Senator, if we could——

Senator BOSCHWITZ. I will conclude with this question.

Senator BAUCUS. Right here, yes.

Senator BOSCHWITZ. I thank you, Mr. Chairman. But let us get the answer to that question. Go right ahead, Mr. Naught.

Mr. NAUGHT. Oh, to answer the question?

Senator BOSCHWITZ. Yes.

Mr. NAUGHT. Well, I do not see it was intentional, but what happened is when the 1981, 1985 Congress chose the target price for corn, and then they asked that the rest of the feed grains be established fair and reasonable. Well, that is where the problem came in on the barley side. They did not take in the Malting side on the target price. They used the Feed side of it. And when they went to calculate the deficiency programs, they threw in the Feed price, which they should have, because they used it on one side of the equation, and then they also threw in the Malting price on that side of the equation. And that is what we say is unfair about it. We do not, as an association do not want to separate out Feed barley, Malt barley, Food barley. We want them—we are a small crop. We understand that. We want to be one crop of barley, but when you look at adjusting the target price, yes, we need to look at the Malting side of it to put it on the target price. We need to look at the Feed side to put in on the target price, and the Food side of it.

If those are added on the target price, then we will live with the price side of it. But what our problem right now is we feel that on one side of the equation is Feed. Other side of the equation is Feed and Malt, and that is not fair. We would like to have Feed and Malt on both sides of the equation.

Mr. LACEY. Right.

Senator BAUCUS. All right. Let us continue with the panel.

Senator BOSCHWITZ. Thank you very much.

Senator BAUCUS. You bet. Thank you very much. Marsha Jones, welcome. Please proceed.

STATEMENT OF MARSHA JONES, NATIONAL GRAINS CHAIRPERSON, WOMEN INVOLVED IN FARM ECONOMICS (WIFE), GROVER, CO

INTRODUCTION

Ms. JONES. I am Marsha Jones. I am national grains chairperson for WIFE, Women Involved in Farm Economics. My husband and I operate a farm and ranch in northeastern Colorado. We produce wheat, barley, oats, cattle, hay, and have done some experimenting with various specialty crops. I am involved with all aspects of the operation from financial planning to operating equipment. I share the decisionmaking responsibility with my husband.

WIFE is a grassroots organization striving to achieve prosperity for agriculture and the Nation through education, communication, legislation and cooperation. WIFE has State associations in 20 States with members at large in nearly every State. WIFE is structured so that there are local chapters, State associations, and the national association. We have a very good working network between the three levels of membership.

I am pleased to have the opportunity to address the subcommittee today on behalf of our WIFE members. I thank you for allowing me this time to present WIFE's concern about the unfair treatment of barley producers by the U.S. Department of Agriculture. This has caused a financial hardship for barley producers throughout the United States, and we thank you for recognizing that there is a problem and arranging this hearing to research solutions to this problem.

CALCULATING TARGET PRICE FOR BARLEY

Our understanding of the method for calculating target price for barley is based on a formula used years ago for determining feed energy value. In the last 20 years, many private and Federal dollars have gone into research to determine the nutritional value for livestock. Research has found that energy is not the only important nutrient that barley can supply. The protein level in barley is very important to the growth and health of livestock. The protein level of barley is 11.6 percent compared to 8.6 percent average for corn. According to the International Mineral Corporation, barley has 93.7 percent of the feed value of corn. According to Ranch-Way Feed Corporation, research has shown that the adjustable fiber in barley when fed to dairy cows is directly related to the butterfat content in their milk.

HAS USDA CALCULATED THE VALUE OF THIS COMMODITY?

Malt barley has a different value that has nothing to do with feed value. Has USDA calculated the value of this commodity?

In calculating the national weighted average price of barley, USDA chooses to use both the Malt barley price and the Feed barley price. If Malting barley is recognized for its dollar value by USDA, why is it not recognized for its food value?

Producers in Colorado will be required to pay back the advanced deficiency payment, approximately $3.5 million. This will be taking needed money out of rural Colorado. This will be the case in all of rural America. It will be taking money off of all main streets of all rural towns.

THE INDIVIDUAL BARLEY PRODUCERS HAVE BEEN FINANCIALLY DEVASTATED BY USDA'S CALCULATION OF THE NATIONAL WEIGHTED AVERAGE PRICE

The individual barley producers have been financially devastated by USDA's calculation of the national weighted average price. Producers are being required to pay back all of the advanced deficiency payment. This has put a financial burden on many producers. The price received by Feed barley producers was considerably less than the national average price. The very deficiency payment designed to protect producers from this inequity in pricing is being taken away.

SINCE THE FARM CRISIS, LENDING AGENCIES HAVE CHANGED THEIR WAY OF DOING BUSINESS

Since the farm crisis, lending agencies have changed their way of doing business. It has taught us all better management skills. One of these skills the agencies demand is the ability to cash-flow. We as producers try to fulfil this obligation. With so many variables that we have no control over, it is difficult. Dry weather conditions have been a major problem. Another added problem is the infestation of the Russian wheat aphid, and now the unfair treatment by USDA. Our bank prefers that we do not put any Government payments in our cash-flow except for Conservation Reserve Program payments. Their feeling is that this is an unreliable source of income. Production loans are made considering all the gambles producers take every year when planting a crop hoping for normal weather conditions and an average income, but that USDA payments are an unacceptable risk.

SENATE BILL 1000 WOULD HELP

Senate bill 1000 would help alleviate the problem for producers in repaying the 1988 and 1989 advanced deficiency payment by excluding the Malt barley price from the national weighted average. Along with this, we need to look ahead to ensure that the barley producers of this Nation receive fair and equitable treatment in the future.

The Federal Government must be fair and reasonable to all barley producers. The Food Security Acts, historically, have been to ensure a reliable food supply for the Nation at a reasonable price. It would be disastrous if this Nation became dependent on a foreign nation for its barley needs because Congress and USDA did not see the value of treating the barley producer in a fair and reasonable manner. We have the ability and the resources to produce barley for our needs. We must not allow this resource to deteriorate to a zero production of barley. Let us not overlook the economical impact barley has on this Nation.

Although Colorado is a real small producing barley State, in 1987 we had 220,000 acres of barley in production, producing 14 million bushels. In 1988 that figure dropped to 175,000 acres, producing 11,725,000 bushels. Again in 1989 the acreage dropped to 160,000 acres. Final production figures are not available yet from the Colorado Department of Agriculture. This is evidence that the barley producer is being treated unfairly, and producers are going to crops that have a better income protection, some by choice, and others by request of their lending agency.

CONCLUSION

WIFE would like to request that Congress instruct USDA to recognize that there are more than one type of barley grown in the

United States with the price differential and to give fair treatment to all of them.

Thank you again Mr. Chairman for allowing WIFE to be represented here.

Senator BAUCUS. Thank you very much, Marsha.

[The prepared statement of Ms. Jones follows:]

WIFE Women Involved in Farm Economics

Marsha Jones
(303) 257-3300

RR2
Grover, CO 80729

UNTIED STATES SENATE
COMMITTEE ON AGRICULTURE, NUTRITION, AND FORESTRY

SUBCOMMITTEE ON AGRICULTURAL PRODUCTION
AND STABILIZATION OF PRICES

REGARDING

BARLEY DEFICIENCY

Oral and Written Testimony

by

Marsha Jones, National Grains Chairperson

Women Involved in Farm Economics

WIFE

April 19, 1990

I AM MARSHA JONES. NATIONAL GRAINS CHAIRPERSON FOR WIFE, (WOMEN INVOLVED IN FARM ECONOMICS). MY HUSBAND AND I OWN AND OPERATE A FARM AND RANCH IN NORTHEASTERN COLORADO. WE PRODUCE WHEAT, BARLEY, OATS, CATTLE, HAY, AND HAVE DONE SOME EXPERIMENTING WITH VARIOUS SPECIALTY CROPS. I AM INVOLVED WITH ALL ASPECTS OF THE OPERATIONS FROM FINANCIAL PLANNING TO OPERATING EQUIPMENT. I SHARE THE DECISION MAKING RESPONSIBILITY WITH MY HUSBAND.

WIFE IS A GRASSROOTS ORGANIZATION STRIVING TO ACHIEVE PROSPERITY FOR AGRICULTURE AND THE NATION THROUGH EDUCATION, COMMUNICATION, LEGISLATION AND COOPERATION. WIFE HAS STATE ASSOCIATIONS IN 20 STATES, WITH MEMBERS AT LARGE IN NEARLY EVERY STATE. WIFE IS STRUCTURED SO THAT THERE ARE LOCAL CHAPTERS, STATE ASSOCIATIONS AND THE NATIONAL ASSOCIATION. WE HAVE A VERY GOOD WORKING NETWORK BETWEEN THE THREE LEVELS OF MEMBERSHIP.

I AM PLEASED TO HAVE THE OPPORTUNITY TO ADDRESS THE COMMITTEE TODAY ON BEHALF OF OUR WIFE MEMBERS. I THANK YOU FOR ALLOWING ME THIS TIME TO PRESENT WIFE'S CONCERNS ABOUT THE UNFAIR TREATMENT OF BARLEY PRODUCERS BY THE UNITED STATES DEPARTMENT OF AGRICULTURE. THIS HAS CAUSED A FINANCIAL HARDSHIP FOR FEED BARLEY PRODUCERS THROUGHOUT THE UNITED STATES. WE THANK YOU FOR RECOGNIZING THAT THERE IS A PROBLEM, AND ARRANGING THIS HEARING TO RESEARCH SOLUTIONS TO THE PROBLEM.

OUR UNDERSTANDING OF THE METHOD FOR CALCULATING TARGET PRICE FOR BARLEY IS BASED ON A FORMULA USED YEARS AGO FOR DETERMINING FEED ENERGY VALUE. IN THE LAST TWENTY YEARS MANY PRIVATE AND FEDERAL DOLLARS HAVE GONE INTO RESEARCH TO DETERMINE THE NUTRITIONAL NEEDS OF LIVESTOCK. RESEARCH HAS FOUND THAT ENERGY IS NOT THE ONLY IMPORTANT NUTRIENT THAT BARLEY CAN SUPPLY. THE PROTEIN LEVEL IN BARLEY IS VERY IMPORTANT TO THE GROWTH AND HEALTH OF LIVESTOCK. THE PROTEIN LEVEL OF BARLEY IS 11.6% ON AVERAGE COMPARED TO 8.6% FOR CORN. ACCORDING TO INTERNATIONAL MINERAL CORPORATION BARLEY HAS 93.7% OF THE FEED VALUE OF CORN. ACCORDING TO RANCH-WAY FEED CORPORATION, RESEARCH HAS SHOWN THAT THE ADJUSTABLE FIBER IN BARLEY WHEN FED TO DAIRY COWS IS DIRECTLY RELATED TO THE BUTTERFAT CONTENT IN THEIR MILK.

MALT BARLEY HAS A DIFFERENT VALUE THAT HAS NOTHING TO DO WITH FEED VALUE. HAS USDA CALCULATED THE FOOD VALUE OF THIS COMMODITY?

IN CALCULATING THE NATIONAL WEIGHTED AVERAGE PRICE OF BARLEY, USDA CHOOSES TO USE BOTH THE MALT BARLEY PRICE AND THE FEED BARLEY PRICE. IF MALT BARLEY IS RECOGNIZED FOR ITS DOLLAR VALUE BY USDA, WHY IS IT NOT RECOGNIZED FOR IT'S FOOD VALUE?

PRODUCERS IN COLORADO WILL BE REQUIRED TO PAY BACK THE ADVANCED DEFICIENCY PAYMENT. APPROXIMATELY $3.5 MILLION. THIS WILL BE TAKING NEEDED MONEY OUT OF RURAL COLORADO. THIS WILL BE THE CASE IN ALL OF RURAL AMERICA. IT WILL BE TAKING MONEY OFF OF ALL MAIN STREETS OF ALL RURAL TOWNS.

THE INDIVIDUAL BARLEY PRODUCERS HAVE BEEN FINANCIALLY DEVASTATED BY USDA'S CALCULATION OF THE NATIONAL WEIGHTED AVERAGE PRICE. PRODUCERS ARE BEING REQUIRED TO PAY BACK ALL OF THE ADVANCED DEFICIENCY PAYMENT. THIS HAS PUT A FINANCIAL BURDEN ON MANY PRODUCERS. THE PRICE RECIEVED BY FEED BARLEY PRODUCERS WAS CONSIDERABLY LESS THAN THE NATIONAL AVERAGE PRICE. THE VERY DEFICIENCY PAYMENT DESIGNED TO PROTECT PRODUCERS FROM THIS INEQUITY IN PRICING IS BEING TAKEN AWAY.

SINCE THE FARM CRISIS, LENDING AGENCIES HAVE CHANGED THEIR WAY OF DOING BUSINESS. IT HAS TAUGHT US ALL BETTER MANAGEMENT SKILLS. ONE OF THESE SKILLS THE AGENCIES DEMAND IS THE ABILITY TO CASH FLOW. WE AS PRODUCERS TRY TO FULFILL THIS OBLIGATION. WITH SO MANY VARIABLES THAT WE HAVE NO CONTROL OVER IT IS DIFFICULT. DRY WEATHER CONDITIONS HAVE BEEN A MAJOR PROBLEM, ANOTHER ADDED PROBLEM IS THE INFESTATIONS OF THE RUSSIAN WHEAT APHID, AND NOW THE UNFAIR TREATMENT BY USDA. OUR BANK PREFERS THAT WE DO NOT PUT ANY GOVERNMENT PAYMENTS INTO OUR CASH FLOW EXCEPT CONSERVATION RESERVE PROGRAM PAYMENTS. THEIR FEELING IS THAT THIS IS AN UNRELIABLE SOURCE OF INCOME. PRODUCTION LOANS ARE MADE CONSIDERING ALL THE GAMBLES PRODUCERS TAKE EVERY YEAR WHEN PLANTING A CROP, HOPING FOR NORMAL WEATHER CONDITIONS AND AN AVERAGE INCOME, BUT THAT USDA PAYMENTS ARE AN UNACCEPTABLE RISK.

SENATE BILL 1000 WOULD HELP ALLEVIATE THE PROBLEM FOR PRODUCERS IN REPAYING THE 1988 AND 1989 ADVANCED DEFICIENCY PAYMENT BY EXCLUDING THE MALT BARLEY PRICE FROM THE NATIONAL WEIGHTED AVERAGE. ALONG WITH THIS WE NEED TO LOOK HEAD TO INSURE THAT THE BARLEY PRODUCERS OF THIS NATION RECEIVE FAIR AND EQUITABLE TREATMENT IN THE FUTURE.

THE FEDERAL GOVERNMENT MUST BE FAIR AND REASONABLE TO ALL BARLEY PRODUCERS. THE FOOD SECURITY ACTS HISTORICALLY HAVE BEEN TO INSURE A RELIABLE FOOD SUPPLY FOR THE NATION AT A REASONABLE PRICE. IT WOULD BE DISASTROUS IF THIS NATION BECAME DEPENDENT ON A FOREIGN NATION FOR ITS BARLEY NEEDS BECAUSE CONGRESS AND USDA DID NOT SEE THE VALUE OF TREATING THE BARLEY PRODUCER IN A FAIR AND REASONABLE MANNER. WE HAVE THE ABILITY AND THE RESOURCES TO PRODUCE BARLEY FOR OUR NEEDS. WE ,MUST NOT ALOW THIS RESOURCE TO DETERIORATE TO A ZERO PRODUCTION OF BARLEY. LETS NOT OVER LOOK THE ECONOMICAL IMPACT BARLEY HAS ON THIS NATION.

IN 1987 COLORADO HAD 220,000 ACRES OF BARLEY IN PRODUCTION, PRODUCING 14,520,000 BUSHELS. IN 1988 THAT FIGURE DROPPED TO 175,000 ACRES, PRODUCING 11,725,000 BUSHELS. AGAIN IN 1989 ACREAGE DROPPED TO 160,000. FINAL PRODUCTION FIGURES ARE NOT AVAILABLE YET FROM THE COLORADO DEPARTMENT OF AGRICULTURE. THIS IS EVIDENCE THAT THE BARLEY PRODUCER IS BEING TREATED UNFAIRLY, AND PRODUCERS ARE GOING TO CROPS THAT HAVE A BETTER INCOME PROTECTION, SOME BY CHOICE, AND OTHERS BY REQUEST OF THEIR LENDING AGENCY.

WIFE WOULD LIKE TO REQUEST THAT CONGRESS INSTRUCT USDA TO RECOGNIZE THAT THERE ARE TWO TYPES OF BARLEY GROWN IN THE UNITED STATES WITH A PRICE DIFFERENTIAL AND TO GIVE FAIR TREATMENT TO THEM BOTH.

THANK YOU AGAIN MR. CHAIRMAN FOR ALLOWING WIFE TO BE REPRESENTED HERE.

Senator **Baucus**. Next, Stephen Naught. Steve.

STATEMENT OF STEPHEN NAUGHT, VICE PRESIDENT, NATIONAL BARLEY GROWERS ASSOCIATION, BICKLETON, WA

Mr. **Naught**. Senator, thank you.

INTRODUCTION

The National Barley Growers Association (NBGA) is pleased to be here today to discuss correcting the two greatest inequities of the Food Security Act of 1985 and of the proposed 1990 Food Security Act. Namely, discrepancies in the calculation of the barley target price and the barley deficiency payments.

My name is Stephen Naught. I am a barley grower from the State of Washington and am presently vice president of the National Barley Growers Association. We are 16 months old. The National Barley Growers Association represents producers in six States that market over 75 percent of all barley produced in the United States.

To reemphasize my opening statement, we cannot stand idly by and watch while the U.S. barley industry literally goes bankrupt. It is time to address the causes of this potential bankruptcy.

FIRST ISSUE THAT MUST BE ADDRESSED AND RECTIFIED

The first issue that must be addressed and rectified is the process the U.S. Department of Agriculture (USDA) uses to calculate barley deficiency payments. The Food and Agricultural Security Acts of 1981 and 1985 established the target price for corn. Regulations then provided that target prices for other feed grains were to be established by USDA using "Fair and reasonable" levels of comparison to the corn target price. Based on these assumptions, USDA established criterion for barley target levels on bushel weight comparisons to corn; i.e., corn 56 pounds compared to barley's 48 pounds. On the surface, this method may appear equitable. However, it does not take into account cost of production, the true feed value of barley, or the value of barley as a food source when establishing the barley target price. The formula they used did not take into account the total nutritional value of barley in the same way that the marketplace does.

To compound the problem and make it even worse, in calculating the deficiency payment, the national weighted average market price for Malting barley was added into the Feed barley national weighted average market price to arrive at an all barley price. This practice caused an unnatural skewing of the average cash price to the high side inasmuch as the premium Malting barley price was not used to establish the target price.

Malting barley has nothing to do with Feed barley. It is like comparing Republicans and Democrats—they are both politicians, but they do not share the same bed politically.

The difference between Malting barley and Feed barley is that Malt——

Senator **Baucus**. They are both very nutritional. [Laughter.]

Go ahead.

Mr. NAUGHT. The difference between Malting barley and Feed barley is that Malting barley is a specialty crop. Because it is produced for a specific market, it must meet rigid quality specifications. Because of these unique quality factors, Malting barley usually commands a price premium over Feed barley. Under normal conditions, the Malting barley premium prices to 1988–89 crops have averaged about 25 to 35 cents per bushel above the price of Feed barley.

The drought conditions of 1988 and 1989 were most severe in the Midwest, the major U.S. Malting barley producing area. Because of the reduced supplies, real or imaginary, the spread between Feed barley price and Malting barley price at times were as high as $2 to $2.50 per bushel at the local level. This abnormal spread caused an equally unnatural skewing of the calculations in determining deficiency payments for 1988 and 1989 and very probably for 1990. The drought inflated price for Malting barley was treated as if it were for all barley, including Feed barley which was a fallacy. Feed barley remained at a more normal price. This is the inequity that we are asking you to repair.

BARLEY GROWERS FACE TWO SPECIAL PROBLEMS

Barley growers face two special problems. The most critical is the repayment of the 1988–89 barley advanced deficiency payment.

Senate bill 1000 offers the least painful solution as it would remove the Malting barley price from the barley deficiency payment calculations. Under the bill, barley growers would still have to repay 8 cents of the 30 cents 1988 advance. It is interesting to note that corn is also repaying 8 cents. Aligning the calculations so they would be equitable would aid the vast majority of growers, especially those who received a market price well below the USDA's established target price. This is only a fair solution for barley growers given inequities with the past methods used to establish target prices.

The second problem is the potential treatment of barley in the 1990 farm program.

We understand Congress faces a huge budget deficit which makes the request for a decent target price for barley a very difficult option. In defense of the request for equality, I ask the Senators to please remember that the barley industry is at a crossroads. During the tenure of the last two farm bills, we have endured target prices well below our cost of production while other program crops enjoyed target prices at or above cost of production. An example, the 1980 target price for barley and corn were approximately 80 percent of cost of production. At the same time the target for wheat was 89 percent of the cost of production. Today, the barley target price is 73 percent of the cost of production, assuming normal yields. At the same time that the target for corn is at 112 percent.

Today, under normal production, the cost of production for barley equates to $3.25 per bushel national average. The target price, however, is set at $2.36 per bushel, 89 cents below the cost of production.

All we ask is that the barley industry is treated, truly treated as Congress intended, that the program be "fair and reasonable." We are not advocating a reduction in the level of target prices for other program crops, but we do ask that the target price be realigned to reflect parity with other program crop levels. If we do not obtain a more equitable target price in the 1990 farm bill, the barley industry will continue to decline in the United States and the balance of agricultural commodities will be severely affected. This domino effect will bring about other economic problems within agricultural world.

Surely, the original intent of Congress in establishing this program was to provide an equitable degree of income protection among commodities by providing deficiency payments based on target prices. It was supposed to provide this equitable degree of income protection among commodities by using the level of payments for each commodity by itself in relation to its cost of production. While the inequities in the 1981 and 1985 Food Security Acts were unintentional, they have had devastating consequences for the barley producers.

Farmers have had strong incentives to produce crops that have high target prices relative to costs, especially if their land allows such diversity. They have much less, if any, incentive to produce crops with low target prices relative to costs: namely, barley and oats. This has produced a tremendous hardship for farmers who cannot grow a wide variety of crops but must depend upon such crops as barley to survive. Regulations of the farm bill have been so discriminatory against barley that the acreage has declined 32 percent since 1985. National barley acreage now totals less than 9 million acres.

CONCLUSION

In conclusion, I ask you to right this wrong and reestablish barley as a viable agricultural commodity by modifying congressional and USDA policies to give barley an equitable chance. Every program crop in the 1981 act enjoyed a substantial increase in target prices except barley and oats. Barley received no target price increase in the 1981 act, nor were any positive changes forthcoming in the 1985 act, however, barley needs your help now. Please consider the American barley producer as important as the producers of other commodities and act quickly to save our industry.

The National Barley Growers Association specifically asks for the following in the Food, Agriculture, Conservation, and Trade Act of 1990:

One, the establishment of the target price for barley based on the cost of production based on a 5-year average.

If that is unacceptable, then at the very least the target price should be based on the total nutritional value of barley with a factor for Malt barley included in the target price calculations.

When nutritional value and the Malting barley factor are included in this calculation and compared to corn's $2.75 per bushel target price, barley's target price should be $2.70. I have included an attachment how we arrived at that issue looking at the total nutritional value.[20]

Also, two, barley needs its own section within the feed grain title to address our unique crop.

Thank you, and I would be happy to answer questions.

Senator BAUCUS. Thank you very much.

[The prepared statement and attachments of Mr. Naught follow:]

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[20] The attachment, "Evaluation of Barley Target Price Utilizing Nutritional Analysis and Market Data" with tables 1-5 and figure 1 can be found on pages 420-428.

STATEMENT OF

STEPHEN NAUGHT
DIRECTOR
WASHINGTON BARLEY COMMISSION
&
VICE PRESIDENT
NATIONAL BARLEY GROWERS ASSOCIATION

BEFORE THE
SUBCOMMITTEE ON AGRICULTURAL PRODUCTION
&
STABALIZATION OF PRICES
UNITED STATES SENATE

REGARDING:

1988 AND 1989 BARLEY DEFICIENCY REPAYMENT
&
BARLEY POSITION IN 1990 FARM PROGRAM

THURSDAY, APRIL 19, 1990

Mr. Chairman and distinguished Senators:

The National Barley Growers Association (NBGA) is pleased to be here today to discuss correcting the two greatest inequities of the 1985 Food Security Act (FSA) and of the proposed 1990 FSA. Namely discrepancies in the calculation of barley target price and barley deficiency payments.

My name is Stephen Naught. I am a barley grower from the state of Washington and am presently Vice President of the National Barley Growers Association. The National Barley Growers Association represents producers in six states that market over 75% of all barley produced in the United States.

To reemphasize my opening statement, we can not stand idely by and watch while the United States barley industry literally goes bankrupt. It is time to address the causes of the potential bankruptcy.

The first issue that must be addressed and rectified is the process the United States Department of Agriculture (USDA) uses to calculate barley deficiency payments. The Food and Agricultural Security Acts of 1981 and 1985 established the target price for corn. Regulations then provided that target prices for other feed grains were to be established by USDA using "Fair and reasonable" levels of comparison to the corn target price. Based on these assumptions, USDA estabished criterion for barley target levels on bushel weight comparisons to corn; ie - corn 56#/bu compared to barley 48#/bu. On the surface, this method may appear equitable, however, it does not take into account cost of production, the true feed value of barley or the value of barley as a food source, when establishing the barley target price.

The formula used did not take into account the total nutritional value of barley in the same way that the market place does. To compound the problem and make it even worse, in calculating the deficiency payment, the national weighted average market price for malting barley was added into the feed barley national weighted average market price to arrive at an all barley price. This practice caused an unnatural skewing of average cash price to the high side in as much as the premium malting barley price was not used to establish the target price.

Malting barley has absolutely nothing to do with feed barley. This is like comparing Republicans and Democrats -- they are both politicians, but do not share the same bed politically.

The difference between malting barley and feed barley is that malting barley is a speciality crop. Because it is produced for a specific market it must meet rigid quality specifications. Because of these unique quality factors, malting barley usually commands a price premium over feed barley. Under normal conditions, the malting barley premium prior to 1988-89 crops had averaged about 25 cents per bushel above the price of ordinary barley.

The drought conditions of 1988 and 1989 were most severe in the midwest, the major U.S. malting barley producing area. Because of reduced supplies, real or imagined, the spread between feed barley price and malting barley price at times were as high as $2.00 to $2.50 per bushel at the local level. This abnormal spread caused an equally unnatural skewing of calculations in determining deficiency payments for 1988 and 1989 and very probably for 1990. The drought inflated price for malting barley was treated as if it were for all barley, including feed barley, which was a fallacy. Feed barley remained at a more normal price. This is the inequity we are asking you to repair.

Barley growers face two special problems. The most critical is the repayment of the 1988 and 1989 barley advanced deficiency payment. Senate Bill 1000 offers the least painful solution as it would remove the malting barley price from the barley deficiency payment calculations. Under the Bill, barley growers would still have to repay eight cents of the 30.4 cent 1988 advance. (It is interesting to note that corn is repaying eight cents.) Aligning the calculations so they would be equitable would aid the vast majority of growers, especially those who received a market price well below the USDA established target price. This is only a fair solution for barley growers, given the inequities with past methods used to establish target prices.

The second problem is potential treatment of barley in the 1990 Farm Program.

We understand, Congress faces a huge budget deficit which makes the request for a decent target price for barley a difficult option. In defense of the request for equality, I ask the Senators to please remember the barley industry is at a crossroad. During the tenure of the last two Farm Bills, we have endured target prices well below our cost of production while other program crops enjoyed target prices at or above cost of production. An example, the 1980 target prices for barley and corn were approximately 80 percent of the cost of production, at the same time the target for wheat was about 89 percent the cost of production. Today the barley target price is 73 percent the cost of production, assuming normal yield. At the same time the target for corn is 112 percent and wheat 88 percent the cost of production.

Today, under normal production regimes, the cost of production for barley equates to $3.25 per bushel national average. The target price, however, is set at $2.36 per bushel, 89 cents below production costs.

All we ask is that the barley industry is truly treated as Congress intended, that the program be "fair and reasonable". We are not advocating a reduction in the level of target prices for other program crops, but we do ask that our target price be realigned to reflect parity with other program crop levels. If we do not obtain a more equitable target price in the 1990 Farm Program, the barley industry will continue to decline in the United States and the balance of agricultural commodities will be severely affected. This domino affect will bring about other economic problems with the agricultural world.

Surely the original intent of Congress in establishing this program was to provide an equitable degree of income protection among commodities by providing deficiency payments based on target prices. It was supposed to provide this equitable degree of income protection among commodities by using the level of payments for each commodity by itself in relation to its own production costs. While the inequities in the 1981 and 1985 Food Security Acts were unintentional, they have had devastating consequences for the barley producers.

Farmers have had strong incentives to produce crops that have high target prices relative to costs, especially if their land allows such diversity. They had much less, if any, incentive to produce crops with low target prices relative to costs: namely barley and oats. This has produced a tremendous hardship for farmers who cannot grow a wide variety of crops, but must depend upon such crops as barley to survive. Regulations of the farm bills have been so discriminatory against barley that the acreage has declined 32 percent since 1985. National barley acreage now totals less than nine million acres.

In conclusion, I ask you to right this wrong and reestablish barley as a viable agricultural commodity by modifying Congressional and USDA policies to give barley an equitable chance. Every program crop in the 1981 Act enjoyed a substantial increase in target price except barley and oats. Barley received no target price increase in the 1981 Act, nor were any positive changes forthcoming in the 1985 Act, however, barley needs your help now. Please consider the American barley producer as important as the producers of other commodities and act quickly to save our industry.

The National Barley Grower Association are specifically asking for the following in the 1990 Food Security Act:

1. The establishment of the target price for barley upon its cost of production, based on a 5-year average.

   If that is unacceptable, then at the very least, the target price based the Total Nutritional value of barley with a factor for malt barley included in the target price calculations.

   When nutritional value and the malting barley factor are included in this calculation and compared to corn's $2.75/bu target price, barley's target price would be $2.70/bu. (See attachment #1.)

2. Barley needs its own section within the Feed Grains title to address our unique crop.

Thank you and I would be happy to answer any questions.

EVALUATION OF BARLEY TARGET PRICE UTILIZING NUTRITIONAL ANALYSIS AND MARKET DATA

Target price of barley is currently set using the corn target rate level adjusted for the weight difference between the two commodities (barley = 48 pounds, corn = 56 pounds per bushel). Inherent in this procedure is the concept that both barley and corn are feed products, consequently, the thought is these commodity relationships should prove equitable. This practice, however, underestimates the true value of barley as a program crop due to the differing feed values of the two commodities as well as marketing and use requirements of barley.

Several factors need to be assessed to accurately reflect the true value of barley as a program crop including:

1. Bushel weight difference between corn and barley,
2. End-use markets,
3. Feed value relationships between corn and barley by livestock species, and,
4. Malting barley premium.

Only the bushel weight difference is considered under the present day target price formulation. Using the process as outlined above, the target price for barley would equate to $2.70 per bushel in 1990 as compared to the current rate of $2.36 per bushel (Table 7).

The following discussion describes a relatively simple process which incorporates historic price and use data along with Partial Nutritional Values to develop a more accurate reflection of an appropriate target price for barley.

Estimates indicate approximately 29 percent of the barley used over the past five marketing years (1984/85 through 1988/89) was used in the production of malt, with the remainder used primarily as feed (Table 1). This assumes that all barley in the Food, Alcohol, & Industrial sector was for malting purposes, while all exported barley was of feed quality.

Malting barley producers received an average premium of $.39 per bushel over feed barley producers for the same time period (Table 2).

The percentage information of barley fed to specific livestock classes was obtained from personal conversation with Linwood Hoffman, ERS, USDA (Table 3). These data were developed in the early 1980's and may be subject to scrutiny, but present the best data available. The 11 livestock classes used in their work were reorganized into four categories (Ruminant, non-dairy; Dairy; Chickens; and Swine) for ease of computation and understanding. While feed relationships could be developed for each specific class, the outcome would likely change little.

Selected feed composition data were obtained from the National Research Council's Feed Composition Tables (Table 4). Total Digestible Nutrients (TDN) and crude protein were used in evaluating the feed relationship between corn and barley for the various livestock classes. Nitrogen-corrected metabolizable energy was substituted for TDN in the analysis for chickens since TDN values were not available. While more thorough, in-depth analysis could be conducted which would encompass specific energy levels, amino acid profiles, etc., TDN and crude protein analysis likely would result in similar comparisons.

Soybean meal prices were included in the analysis as a base of comparison for the higher levels of protein in barley versus corn (Table 5).

Partial Nutritional Value (PNV) approach was used to determine barley's feed value in relation to corn (Figure 1). For ease of understanding, PNV essentially compares the difference in TDN and crude protein (CP) between corn and barley. The 1990 corn target price of $2.75 per bushel was used to determine a relative TDN value of barley, while soybean meal price was used to determine the "protein premium" of barley.

The PNV approach was used to determine relative feed values of barley by livestock species, then weighted by the relative proportion fed to each species (Table 6). The feed value of barley based on a $2.75 per bushel corn target price is $2.59 per bushel. The average malting barley premium over the past five marketing years, weighted for it's proportional use, is an additional $.11 per bushel.

The true value of barley as a feed and food source, based on a $2.75 corn target price is $2.70 per bushel.

TABLE 1. BARLEY DISAPPEARANCE, MARKETING YEARS 1984/85 THROUGH 1988/89

Marketing Year	Food, Alcohol & Industrial	Seed, Feed & Residual	Exports	Total Disappearance
	- - - - - - - - - -	million bushels	- - - - - - - - - -	
1984/85	149.0	325.5	76.8	551.3
1985/86	147.2	353.9	21.8	522.9
1986/87	156.1	315.7	136.6	608.4
1987/88	158.3	273.7	126.1	558.1
1988/89	165.7	180.7	84.6	430.0
5-Year Average	155.3	289.9	89.2	534.4

SOURCE: USDA, ERS, Feed Situation and Outlook Report, FdS-312, November 1989.

Proportion of Barley Used By Type, Five-Year Average, (Assumes all barley in Food, Alcohol & Industrial sector is for malting purposes, and all barley in Export sector is of feed quality)

Malting	29%
Feed	71%

TABLE 2. AVERAGE BARLEY PRICE RECEIVED BY FARMERS, MARKETING YEARS 1984/85 THROUGH 1988/89

Marketing Year	All Barley	Feed Barley	Malting Barley
	$/bushel		
1984/85	2.29	2.23	2.38
1985/86	1.98	1.90	2.12
1986/87	1.61	1.52	1.79
1987/88	1.81	1.64	2.01
1988/89	2.79	2.29	3.24
5-Year Average	2.10	1.92	2.31
5-Year Average Malting Premium over Feed			0.39

SOURCE: USDA, NASS, Agricultural Statistics Board, Agricultural Prices 1988 Summary, Pr1-3(89), June 1989.

USDA, NASS, Agricultural Statistics Board, Agricultural Prices, June 29, 1989.

TABLE 3. BARLEY FED BY LIVESTOCK CLASS

Species	Percentage of Use	Recategorized As:*
Milk Cows	33	Dairy
Cattle on Feed	22	Ruminants
Hogs	12	Swine
Hens & Pullets	11	Chickens
Other Beef	10	Ruminants
Other Dairy	3	Dairy
Other Livestock	3	Ruminants
Horses & Mules	2	Ruminants
Other Chickens	2	Chickens
Feed & Stock Sheep	1	Ruminants
Broilers & Turkeys	1	Chickens

SOURCE: Personal conversation with Linwood Hoffman, April 6, 1990. Data provided for marketing years 1982/83 and 1983/84.

* Recategorized totals used to develop feed value of barley:

Ruminants	38%
Dairy	36%
Chickens	14%
Swine	12%

TABLE 4. SELECTED FEED COMPOSITION OF BARLEY, CORN, AND SOYBEAN MEAL, DRY MATTER ON AN AS-IS BASIS

Grain	International Feed Number	Crude Protein	Ruminants (non-dairy)	Dairy	Chickens	Swine
			% TDN	% TDN	ME_n (Mcal/Kg)	% TDN
Barley	4-00-549	11.9	74.0	84	2.51	70.0
Corn	4-26-935	9.6	77.0	80	3.38	80.0
Soybean Meal, 44% Protein	5-20-637	44.0				

SOURCE: National Research Council, United States-Canadian Tables of Feed Composition, 3rd Revision, National Academy Press, Washington, D.C., 1982.

TDN = Total Digestible Nutrients
ME_n = Nitrogen-corrected metabolizable energy

TABLE 5. SOYBEAN MEAL, 44% PROTEIN: PRICES PAID, U.S. BASIS

Marketing Year	Price
	$/cwt
Oct./Sept. 1984/85	10.68
Sept./Aug. 1985/86	11.03
Sept./Aug. 1986/87	11.70
Sept./Aug. 1987/88	19.32
Sept./Aug. 1988/89*	16.20
5-Year Average	13.79

* Simple average estimate of quarterly prices.

SOURCE: USDA, ERS, Feed Situation and Outlook Report, FdS-312, Nov. 1989; FdS-307; Aug. 1988; FdS-303, Sept. 1987; and FdS-300, Aug. 1986.

USDA, NASS, Agricultural Statistics Board, Agricultural Prices, April 30, 1989; July 31, 1989; October 31, 1989.

FIGURE 1. DEVELOPMENT OF FEED VALUE OF BARLEY IN RELATION TO CORN

Corn Price (1990 Target Level)	\$2.75/bu (\$4.91/cwt.)
Soybean Meal (5-Year Average Price)	\$13.79/cwt.

Feed value of barley by livestock species was developed using PNV (Partial Nutritional Value) approach*:

$$V_B = [(TDN_B/TDN_C)*P_C] + [(CP_B - CP_C)/CP_S] * P_S$$

Where:
V_B = Value of barley
TDN_B = Total digestible nutrients of barley
TDN_C = Total digestible nutrients of corn
P_C = Price of corn
CP_B = Crude protein of barley
CP_C = Crude protein of corn
CP_S = Crude protein of soybean meal
P_S = Price of soybean meal

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* In the case of poultry, TDN was replaced by nitrogen-corrected metabolizable energy.

TABLE 6. BARLEY FEED AND MALTING PRICE COMPARISON TO 1990 CORN TARGET PRICE

Livestock Species	Value of Barley	*	Proportion Fed by Species	=	Value by Species
	$/bushel		percent		$/bushel
Ruminants	2.61		38		$0.992
Dairy	2.82		36		1.015
Chickens	2.10		14		0.294
Swine	2.41		12		0.289
Total Feed Value					$2.59
Value of barley as a livestock feed:					$2.59
Malting barley premium: (5-year average malting barley premium of $0.39/bu. * 5-year average malting barley use of 29%)					$0.11
Total Value of Barley (In relation to corn target price of $2.75/bushel):					$2.70

Senator BAUCUS. Thank you very much. Our final witness is Mr. Tim McGreevy.

STATEMENT OF TIM D. McGREEVY, ADMINISTRATOR, IDAHO BARLEY COMMISSION, BOISE, ID

Mr. McGREEVY. Thank you, Senator Baucus.

INTRODUCTION

Mr. Chairman and members of the subcommittee, I am Tim McGreevy from Boise, Idaho. I appear before this subcommittee today representing the Idaho Barley Commission and the Idaho Grain Producers Association.

The issue before this subcommittee today really goes beyond the barley deficiency repayment issue. The real issue for barley growers is: Will the Federal Government treat barley growers in a "fair and reasonable" manner as stated in the text of the 1985 Food Security Act? My comments today are from the perspective of the western barley grower who feels that barley has not been fairly treated in the current farm program.

HISTORICAL PERSPECTIVE

I would like to first go into a little historical perspective. The 1988 and 1989 barley deficiency repayment problem is the result of a policy shift which really began in the 1981 Food Security Act. Prior to the 1981 act, target prices were determined for each commodity based on relative economic cost of production. But, in the 1981 act, Congress moved away from determining target prices based on the cost of production and, instead, wrote specific target prices for each commodity title. In the feed grains title, corn was assigned a specific target price. The title specified that the sorghum, barley, and oat target price would be set in a "fair and reasonable" relationship to the corn target price.

The real problem for barley growers began with the 1981 farm bill. The USDA determined that target prices should better reflect the feed energy value between the feed grains when fed to livestock and poultry. In my prepared testimony, I have chart 1 which demonstrates the result of the USDA's "fair and reasonable" determination for barley. From 1981 to 1984, corn target prices increased by 63 cents per bushel. Sorghum target prices increased by 33 cents per bushel. Barley target prices, as it shows in the graph, during the same period, remained constant. In fact, barley and oats were the only crop commodities in the farm program not to receive an increase in their target price in the 1981 act as the graph indicates.

USDA HAS NOT FULLY ADJUSTED THE TARGET PRICES

It must be noted that the USDA has not fully adjusted the target prices between the feed grains to reflect what they consider the proper feed energy value relationship. But, the USDA's policy of moving toward using feed energy values to determine the target prices between the feed grains is seriously flawed for the following reasons:

USING FEED ENERGY VALUES TO DETERMINE THE TARGET PRICES BETWEEN THE FEED GRAINS IS SERIOUSLY FLAWED

One, in a letter to the National Barley Growers Association, Agriculture Secretary Yeutter stated that the feeding value of barley was about 81 percent of corn. That statement may have been true when it was written 30 years ago. However, current research published by the National Research Council shows that when the total nutritional value of barley is considered, the feeding value of barley is at least equal to, and often exceeds, the feeding value of corn.

Two, currently the USDA uses only feed energy values and totally disregards the higher protein and amino acid balance which actually favor barley in current research. To be truly "fair and reasonable," the USDA should consider the total nutritional value of the commodity, not just its feed energy value.

Three, the USDA fails to include the contribution of Malt barley when it determines the barley target price. Yet, the USDA includes Malt barley prices when calculating the barley deficiency payment as you stated in your opening statement.

Including Malt barley prices in the deficiency payment calculation is especially unjust to Feed barley growers given the current target price inequities. In the States of Oregon, Washington, Idaho, and Montana, over 65 percent of the varieties produced are Feed barley varieties. A Feed barley variety cannot be sold to a Malt barley company for a premium. It is not a Malt barley variety.

Of the varieties produced in the western region 35 percent are Malt barley varieties; but only 25 percent of the 35 percent of that production actually makes it into the malt houses, due to quality factors. The remaining 10 percent of the Malt barley production goes back into livestock feeding channels. So, in Western States, about 75 percent of the barley that is produced is Feed barley. The vast majority of the barley growers in the West will never receive a Malt barley premium.

In Western States, Feed barley prices were over 25 cents a bushel below the barley target price in 1988 and 1989. Yet, these farmers are being asked to repay their entire advanced deficiency payment.

Barley program signup numbers are considerably lower than other commodities. For example, in 1989, only 50 percent of the total barley base in Idaho was signed up for the feed grains program. Irrigated barley growers with Malt barley contracts left the farm program because it offered very little income protection. Yet, those irrigated Malt barley growers in my State who are out of the farm program still influence the deficiency payment received by the barley growers in the farm program. Nationally, only 68 percent of the effective barley base was enrolled in the farm program in 1989, 68 percent. The effective barley base enrolled in the corn program was 81 percent; in the cotton program, 89 percent; in the rice program, 94 percent. The enrollment figures are higher than barley in these commodities because the farm program offers these growers greater income protection.

One purpose of the farm program is to ensure relative price stabilization and adequate supplies of the major farm program commodities. When participating in the farm program, a farmer must leave ground idle, meet conservation objectives, and many other guidelines. In exchange for meeting the guidelines, a farmer is offered a level of income protection through the target price. Unfortunately, the current program makes it more attractive to raise certain commodities over others.

CHART 2

In my testimony I have another graph, chart 2, which shows the target price of five program commodities as a percentage of the economic costs of producing those commodities. 100 percent represents where the target price equals the cost of producing the commodity according to the USDA. The target price for barley is clearly below the national average cost of producing a bushel of barley and has been for several years. Corn, sorghum, and wheat have target prices that better reflect the cost of producing those commodities. When a farmer makes a decision on what to plant, he or she naturally bases that decision on what will yield the highest dollar return. In the West, farmers plant as much wheat as they possibly can because the target price is closer to the true cost of production.

The disparity is magnified in the Conservation Reserve Program (CRP). The CRP in Idaho has taken out nearly 20 percent of the total barley base. The CRP has only taken out 13 percent of the total wheat base. Barley and wheat are grown on the same acres Idaho, but farmers always put their barley base in first because it offers less income protection.

CONCLUSION

In conclusion, Mr. Chairman and members of the subcommittee, the barley growers of this country are victims of a poor policy decision that dates back to the 1981 farm bill. Every program crop in the 1981 act enjoyed a substantial increase in target price except barley and oats. Barley and oats received no target price increase in the 1981 act due to a policy that failed to recognize the total nutritional value of barley and its use in the food chain.

BARLEY GROWERS FACE TWO PROBLEMS

Barley growers face two problems, two distinct problems. The first and most immediate is the repayment of the 1988 and 1989 barley deficiency payment. Senate bill 1000 introduced by Senator McClure of Idaho, and others, offers the easiest solution to this short-term problem caused by two severe droughts and an unfair target price. Senate bill 1000 would remove the Malt barley price from 1988 and 1989 barley deficiency payment calculation, as other witnesses have testified.

The second problem is the position of barley in the 1990 farm program. We fully understand that Congress faces a huge deficit which makes the request for this higher target price a difficult option, but members of the committee, barley is at a crossroads. For years, we have endured a target price that is well below our cost of production while other program crops enjoyed a target price at or about their cost of production. We appeal to your sense of fairness. We do not advocate a reduction in the level of target price for other commodities. But we do ask that our target price be raised to better reflect our cost of production so that we may compete on a level playing field with other program commodities. If we do not obtain a more equitable target price in the 1990 farm program, barley acreage will continue to decline in the United States. It will decline not because it is any less competitive than the other program crops, but rather it is not as fairly treated in the farm program.

We were not organized in 1981 to address this problem when it first arose, but we are organized now. And we ask that you help us correct these inequities in the 1990 farm bill.

I would be happy to answer any questions, and I thank the Senators for the opportunity.

Senator BAUCUS. Thank you all very much.

[The prepared statement and charts of Mr. McGreevy follow:]

STATEMENT
OF

TIM D. MCGREEVY, ADM.
IDAHO BARLEY COMMISSION

BEFORE THE
SUBCOMMITTEE ON AGRICULTURAL PRODUCTION
AND STABILIZATION OF PRICES
UNITED STATES SENATE

REGARDING

1988 AND 1989 BARLEY DEFICIENCY REPAYMENT
BARLEY POSITION IN 1990 FARM PROGRAM

APRIL 19, 1990

Mr. Chairman and members of the Subcommittee, I am Tim McGreevy from Boise, Idaho. I appear before this subcommittee today representing the Idaho Barley Commission and the Idaho Grain Producers Association.

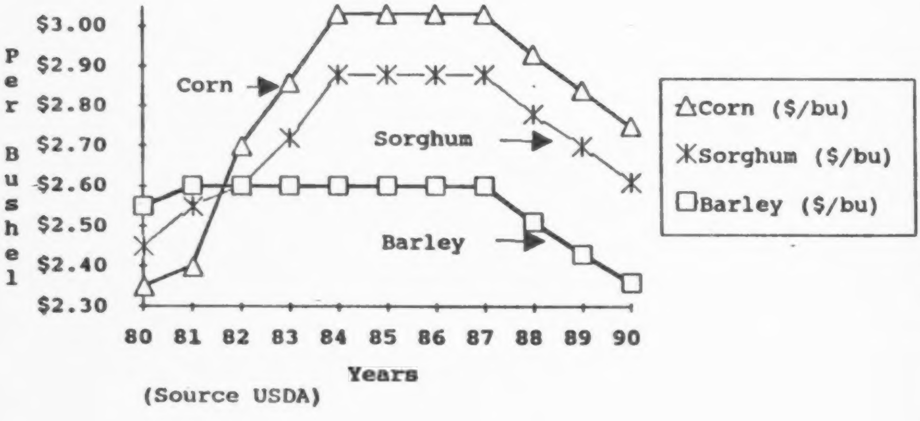
The issue before this committee today goes beyond the barley deficiency repayment issue. The real issue for barley growers is: Will the federal government treat them in a "fair and reasonable" manner as stated in the text of the 1985 Food Security Act? My comments today are from the perspective of the western barley grower who feels that barley has not been fairly treated in the current farm program.

Historical perspective: The 1988 and 1989 barley deficiency repayment problem is the result of a policy shift which began in the 1981 Food Security Act. Prior to the 1981 act, target prices were determined for each commodity based on its relative economic cost of production. But, in the 1981 act, Congress moved away from determining target prices based on the cost of production and, instead, wrote specific target prices for each commodity title. In the Feed Grains title, corn was assigned a specific target price. The title specified that the sorghum, barley, and oat target price would be set in a "Fair and Reasonable" relationship to the corn target price.

The real problem for barley growers began with the 1981 Farm Bill. The USDA determined that target prices should better reflect the feed energy value between the feed grains when fed to livestock and poultry. Chart #1 demonstrates the result of the USDA's "Fair and Reasonable" determination for barley. From 1981 to 1984, corn target prices increased by 63 cents per bushel. Sorghum target prices increased by 33 cents per bushel. Barley target prices, during the same period, remained constant. **In fact, barley and oats were the only crop commodities in the farm program not to receive an increase in their target price in the 1981 act.**

Chart #1

History of Target Prices (1980-1990)



(Source USDA)

It must be noted that the USDA has not fully adjusted the target prices between the feed grains to reflect what they consider the proper feed energy value relationship. **But, the USDA's policy of moving towards using feed energy values to determine the target prices between the feed grains is seriously flawed for the following reasons:**

1. In a letter to the National Barley Growers Association, Agriculture Secretary Yeutter stated that the feeding value of barley was about 81 percent of corn. That statement may have been true when it was written 30 years ago. **However, current research published by the National Research Council shows that when the total nutritional value of the barley is considered; the feeding value of barley is at least equal to, and often exceeds, the feeding value of corn.**

2. Currently, the USDA uses only feed energy values and totally disregards the higher protein and amino acid balance which favors barley. **To be truly "fair and reasonable", the USDA should consider the total nutritional value of the commodity, not just its feed energy value.**

3. **The USDA fails to include the contribution of malt barley when it determines the barley target price. Yet, the USDA includes malt barley prices when calculating the barley deficiency payment.**

Including malt barley prices in the deficiency payment calculation is especially unjust to feed barley growers, given the current target price inequities. In the states of Oregon, Washington, Idaho, and Montana over 65% of the varieties produced are feed barley varieties. A feed barley variety cannot be sold to a malt company for a premium.

Thirty five percent of the varieties produced in the western region are malt barley varieties; but only 25% of that production actually makes it into the malt houses, due to quality factors. The remaining 10 percent of the malt barley production goes back into the livestock feeding channels. **Therefore, in the western states about 75 percent of the barley that is produced is feed barley. The vast majority of the barley growers in the West will never receive a malt barley premium.**

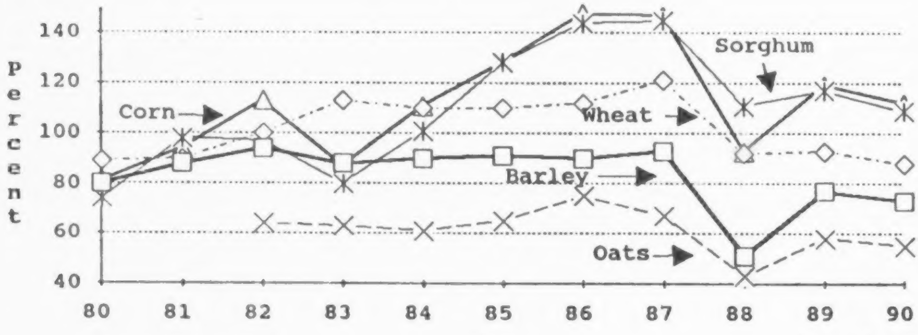
In the western states, feed barley prices were over 25 cents a bushel below the barley target price of 1988 and 1989. Yet, these farmers are being asked to repay their entire advanced deficiency payment.

Barley program sign-up numbers are considerably lower than other commodities. For example: in 1989 only 50% of the total barley base in Idaho was signed up for the feed grains program. Irrigated barley growers with malt barley contracts left the farm program because it offered very little income protection. Yet, those irrigated malt barley growers who are out of the farm program still influence the deficiency payment received by the barley grower in the farm program. **Nationally, only 68% of the effective barley base was enrolled in the farm program in 1989. The effective base enrolled in the corn program was 81%; in the cotton program, 89%; in the rice program, 94%. The enrollment figures are higher than barley in these commodities because the farm program offers these growers greater income protection.**

One purpose of the farm program is to ensure relative price stabilization and adequate supplies of the major program commodities. When participating in the farm program, a farmer must leave ground idle, meet conservation objectives, and many other guidelines. In exchange for meeting the guidelines, a farmer is offered a level of income protection through the target price. Unfortunately, the current program makes it more attractive to raise certain commodities over others.

Chart #2 shows the target price of five program commodities as a percentage of the economic cost of producing those commodities. 100% represents where the target price equals the cost of producing the commodity. The target price for barley is clearly below the national average cost of producing a bushel of barley and has been for several years. Corn, sorghum, and wheat have target prices that better reflect the cost of producing those commodities. **When a farmer makes a decision on what to plant, he or she naturally bases that decision on what will yield the highest dollar return. In the West, farmers plant as much wheat as they possibly can because the target price is closer to the true cost of production.**

Chart
#2
TARGET PRICES AS A PERCENTAGE OF ECONOMIC COST OF
PRODUCTION



(Source USDA) (89,90-Proj.)

The disparity is magnified in the Conservation Reserve Program (CRP). The CRP in Idaho has taken out nearly 20% of the total barley base. The CRP has only taken out 13% of the total wheat base. Barley and wheat are grown on the same acreage in Idaho, but farmers always put their barley base in first because it offers less income protection.

In conclusion, Mr. Chairman and members of the Subcommittee, the barley growers of this country are victims of a poor policy decision that dates back to the 1981 Farm Bill. Every program crop in the 1981 act enjoyed a substantial increase in target price, except barley and oats. **Barley and oats received no target price increase in the 1981 act due to a policy that failed to recognize the total nutritional value of barley and its use in the food chain.**

Barley growers face two problems. The first and most immediate is the repayment of the 1988 and 1989 barley advanced deficiency payment. Senate Bill 1000 introduced by Senator McClure and others offers the easiest solution to this short term problem caused by two severe droughts and an unfair target price. SB 1000 would remove the malt barley price from the 1988 and 1989 barley deficiency payment calculation. Under this bill, barley growers would still have to repay 8 cents of the 30.4 cent 1988 advance. This bill would help the vast majority of growers who received a market price well below the USDA established target price.

The second problem is the position of barley in the 1990 farm program. We fully understand that Congress faces a huge deficit, which makes the request for a higher target price for barley a difficult option. But, members of the committee, barley is at a crossroads. For years we have endured a target price that is well below our cost of production, while other program crops enjoy a target price at or above their cost of production. We appeal to your sense of fairness. We do not advocate a reduction in the level of target price for other commodities. **But we do ask that our target price be raised to better reflect our cost of production so that we may compete on a level playing field with the other program commodities. If we do not obtain a more equitable target price in the 1990 farm program, barley acreage will continue to decline in the U.S.. It will decline, not because it is any less competitive than the other program crops; but, rather, it is not as fairly treated in the farm program.**

I would be happy to answer any questions you may have.

Senator BAUCUS. Earlier, Senator Boschwitz asked a question of you, George. I would like to address it to all of you. His question concerned the fact that there are variations among different commodities, cotton, for example, and wheat. I take it that all of you think that the differences between Malt and Feed barley, not only in drought years but in nondrought years are greater, significantly greater, than are some of the variations among varieties of wheat or cotton, and other commodities. Is that your view, any of you?

Mr. McGREEVY. Mr. Chairman, Senator Baucus, the difference is that Malt barley has a higher percentage of its total crop into this specialty area when compared to other commodities. About 30 percent of our crop does go into the Malt house. Durum wheat is maybe 10 percent of the total wheat production. But the real issue is when the wheat target price was established. Durum was considered, but in barley, Malt barley was not considered in the target price. See? Wheat got a target price of $4.23 when they originally did it in 1985, but we did not. We received a target price based on Feed, and our Malt was not included in the target price. That is what we are arguing. We are not arguing—yes, Mr. Bjerke does bring up a good point when he says, well, other commodities are going to be clamoring in. What we are complaining about is we were not in to begin with.

Senator BAUCUS. Would you agree that the differences between Malt and Feed barley is greater than between Durum and other forms of wheat?

Mr. NAUGHT. Senator, I would disagree with that in the aspect that when the Malting barley is seeded, it has to be treated as barley because it will not make Malting barley until after it is made. You take North Dakota which we consider a Malting barley State, but still 60 percent of their production is going to go to Feed. So they are actually a Feed State, but when they seed it, they are hoping to be able to meet these rigid characteristics and make that Malting for the extra premium.

Senator BAUCUS. That is right, but they use certain practices hoping that it is Malting barley.

Mr. NAUGHT. That is correct. That is exactly right.

Senator BAUCUS. But it may not be.

Mr. NAUGHT. That is correct. That is right. So we are not advocating in the 1990 farm bill of separating Malt and Feed. We want them together because we are a small crop. We feel that way. All we are saying is——

Senator BAUCUS. You want them together both for the purposes of determining a target price as well as market?

Mr. NAUGHT. Yes, sir.

Mr. McGREEVY. If we were included on the front-end, if we were included, our total nutritional value of Feed barley was included, plus the Malting barley factor, we would accept the national, the all barley price that Mr. Bjerke spoke of. But they are not on both sides of the equation right now. And so I know the issue is a bit confusing because in 1988–89 we are asking Malt barley to be dropped out.

Senator BAUCUS. Right.

Mr. McGREEVY. But that is a short-term solution. It is the easiest solution we could think of to handle the problem. We could hardly increase the target price because that would be more budget exposure.

Senator Baucus. Are the barley producers throughout the country generally in agreement about dropping out for purposes of deficiency payment but lumping together for purposes of the 1990 farm bill?

Mr. McGreevy. That is correct.

Mr. Naught. Yes.

Mr. Lacey. Yes, sir.

Senator Baucus. All agreed?

Senator Gorton. All agreed.

Mr. Lacey. All States have voted on that, yes.

Senator Baucus. OK.

Mr. McGreevy. Yes.

Senator Baucus. All right. Yes.

Mr. Lacey. In the Midwest, we have the Red River Valley, Minnesota, North Dakota. Sure, the rest of North Dakota raises a lot of barley. But with that 20 cents or 25 cents differentiation between Malting and Feed, which does not amount to a lot, but some people head for it. And it is worth heading for. But if you are truly going to head for it, then you truly have to make an effort, and it truly costs you something more. So you may end up with a slightly higher net if you make Malt, but Mother Nature has so much to do with it. I get a good nitrogen bearing rain, showers, you know, directly, hey, Mother Nature gave me too much rain, too much nitrogen, and I end up with more protein than I can handle no matter what I did.

So what I am saying is the net dollars per acre are not that much different because we do manage it differently if we truly head for Malting barley even in the Midwest. And more and more of us are learning how we can influence the outcome of what we hope will be Malting barley. We used to, all of us in the Midwest, planted Malting barley in the spring, knowing full well that in the fall two-thirds of us would be disappointed because only a third could be used in the Malting trade. The Malting trade could only assume one-third of the bushels. That is all there is room for. I do not care if the entire crop qualified and would make good Malt, they can only use one-third of the production. So, you know, it is a real quandary. But that is not that much difference to try and sort it out.

Senator Baucus. You heard Administrator Bjerke say that it will be a little complex.

Mr. Lacey. Again, I do not think so.

Senator Baucus. In a nutshell, how do you propose that the value of Malting barley be included in the calculation of the target price?

Mr. Lacey. Just as Mr. Naught has in his testimony.

Senator Baucus. Sorry?

Mr. Lacey. Just as Mr. Naught has in his testimony.

Senator Baucus. Could you explain that again, please, Mr. Naught?

Mr. Naught. Well, in our testimony we showed the very last page, we came up, if you look at the total nutritional value, we are comparing this to $2.75 corn. The total nutritional value of barley as feed, we broke it down to the classes of livestock, just the way the market looks at it, just the way the nutritionists run it through their costs, least cost rations. It would come to $2.59. We looked at taking the Malting barley, took a 5-year average, and divided that out, and it came to 11 cents.[21]

We said, OK, we will live with that 11 cents added on to the end of the target price and accept the higher Malt because we feel the Malt grower is a barley grower. So that is how we did it.

Senator BAUCUS. I am just trying to anticipate what objections we might meet when we in the committee go to markup and propose this. What are some of the legitimate objections that we are going to front up against?

Mr. NAUGHT. Well, I think——

Senator BAUCUS. They are not legitimate obviously, but, what am I going to hear?

Mr. NAUGHT. The ones you hear? I think the one that really hurts is they say—and I am not a Malting barley grower——

Senator BAUCUS. No.

Mr. NAUGHT. I am a Feed grower. But I always hear that the Malting barley grower is going to make a killing if you take the Malting barley out of Senate bill 1000. Well, they are not going to make a killing. They really got hurt, as Mr. Paul had mentioned, their crops were way down on production. Even if they got a large price, they did not have anything to sell. You throw in this "windfall profit" and their income is still way down. So that is not a true statement. They are not making a windfall profit.

Senator GORTON. They only get a real high price if they have not produced that much?

Mr. NAUGHT. That is exactly right. If there is a drought. Right.

Mr. LACEY. And you add a drought in 1988 and 1989.

Senator BAUCUS. Exactly. OK. Senator Gorton. Thank you.

Mr. NAUGHT. Thank you.

Senator GORTON. Mr. Naught—you or any of you can answer this question—with respect to the first question, it comes right down to this. A repayment of the deficiency payment is designed to make up a difference between that payment and what you actually received for a crop and what you are complaining about is that you are being required now to make up for a fictional difference because you could not possibly sell your Feed barley for the price upon which this deficiency payment is based; is that not a summary of the whole thing?

Mr. NAUGHT. Yes, very correct, Senator.

Senator GORTON. You would be required to pay real money for a fictional amount of money that you were never able to get from the crop in the first place?

Mr. NAUGHT. That is correct.

Senator GORTON. I think you may have said this in the course of your testimony, but I think it is important for us to have on the record. We know what your druthers are, but if you can reach only one of these two goals, which is the more important?

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[21] See p. 428.

Mr. NAUGHT. That is a tough question. I guess the bottom line is if we are talking flexibility and looking to the future, unless we get barley's target price up there in line with other crops, we are not even in the ballpark. Oats has already fallen off the table. We are importing oats into this country, you know. Now barley is at the end of the table, and if we do not get them up in line with the other commodities, we are dead. So I guess we would have to say we want to be treated fair and reasonable.

Senator GORTON. As far as the future is concerned?

Mr. NAUGHT. That is correct. We have had 10 years——

Senator GORTON. Let me give you the opportunity to put this down.

Mr. NAUGHT. OK.

Senator GORTON. Why should Members of the U.S. Senate or the Senate Agriculture Committee care whether you grow barley or have to grow something else?

Mr. NAUGHT. I guess why do you care if you grow wheat, cotton, corn or the other crops?

Senator GORTON. No, I hope that is not the answer. I mean assuming that you can go over to some other kind of thing, why should we care whether you as an individual are growing barley or wheat?

Mr. NAUGHT. Because barley is a very vital industry. We have an excellent nutritional value for our livestock. Our livestock gain well on barley. It is a place for that.

Senator GORTON. And because if you go out of the business we are going to end up being importers?

Mr. NAUGHT. That is exactly right. Same as corn. I mean same as oats have done.

Senator GORTON. OK.

Mr. NAUGHT. And then what is amazing is that we are going to move into wheat, and that is going to cause wheat problems.

Mr. MCGREEVY. That is right.

Mr. NAUGHT. Wheat, if they can move into corn, are going to cause corn problems. It is just a domino effect.

Senator GORTON. All right. We wanted that on the record. I have one final question for you all to answer, and this is probably the most difficult. Several of you have been powerful, you have been tough, and you have said you do not want us to have to, you know you do not want this money to come out of the pockets of wheat growers or cotton growers or anyone else. You just want justice. Our problem is the money is going to come out of somebody else's pocket. We are going to be given so many dollars that we can spend, you know, on the entire farm bill, and we are not going to be able to get from here to there unless we figure out how to pay for it.

In a sense, I just want you to understand that. In another sense, you really probably do have to come up with some suggestion for us in a way to find the money from some lower priority field within agriculture if we are going to be able to be successful in helping you out. I hope that is not the case. I would like to be able to just do what you want to do, but we are going to get the end of what we are working on now, and we are going to find that we are way over the amount of money that the farm bill is going to be able to carry this year, and we are going to have to start chopping back. So as eloquently—and Mr. McGreevy, you put this marvelously. I think you did, too, Mr. Naught. The hard truth of it is we are still going to have to find this money someplace within agriculture. And let me just tell you if you have some suggestions for that, we certainly need them.

Mr. NAUGHT. Well, I guess we have to meet that reality, and it is a tough reality, and we are concerned about that. I guess what we are saying is get the playing field level and then we will all take our cuts together. But right now if it is not level and we take our cuts at an unlevel layer, we are out the door, we are off the table.

Senator GORTON. That is unfortunate. It is unfortunate that you are a very small program crop, and you are a bunch of a little kids in a playpen with a bunch of big kids.

Mr. NAUGHT. That is exactly right.

Mr. MCGREEVY. We kick hard, though.

Mr. PAUL. Senator, I would like to mention one thing, if I may. Senator, as far as where does the money come from, and this is not necessarily in the form of a suggestion but at least a reminder that, you know, agriculture took its hit already and early on in some of the statements we were talking about the disaster legislation in 1988, and I simply want to remind all of us that at that time there was a deficiency payment savings of several dollars, and in the beginning, as my memory, and it may be somewhat faulty, but at the time when they originally started looking at that legislation, there was talk of somewhere in the vicinity of $12 billion, I think it was $12 to $15 billion that were going to be available from various deficiency payments that were not going to be made. And that money would be available to help out in the disaster legislation, and of course, as you know, it came down.

Senator GORTON. Absolutely true, but that was based on a farm bill and a budget that we had already passed, and it happened afterwards. When we pass this bill, we have to assume that whatever we put in is going to be spent.

Mr. PAUL. True. But the only point that I want to make, sir, is that, and respectfully so, is that those were allocated agricultural dollars that to my knowledge at least have never been spent in agriculture. So they want to take a cut, you know, before they go looking for a cut in agriculture, they might find another place to do it.

Senator GORTON. Mr. Lacey had his hand up.

Mr. LACEY. Yes, Senator, I think as a farmer in the Midwest who is able to grow corn, wheat or barley and appreciate the opportunity to rotate, without some help in aligning the target price on barley, I will be forced into a lesser rotation because I have the opportunity to only participate then in a couple of crops instead of—and I think that is not fair to barley because I can do a good job with barley. We need to have that opportunity, but the economics of it are that unless we can get the $2.70 I will not grow it.

Senator GORTON. Mr. Chairman, thanks.

Senator BAUCUS. Yes, I think there is another point or two on the budget. From 1980 to present, in real terms, price supports in agriculture have been the fastest declining part of the Federal budget. Farmers have already suffered major hits over the last several years in real terms.

You have all been very helpful here. I must say that you were all very articulate. Several of the Senators have been passing me notes saying how articulate all of you are. That is good. Thank you very much for your testimony. We will work hard, several of us on this committee, to make sure that both of the problems you have addressed, the deficiency as well as the formula, are addressed in the 1990 farm bill. It is very important they both be addressed. Thank you very much.

Mr. LACEY. Thank you.

Mr. NAUGHT. Thank you, Senator.

Senator BAUCUS. You bet.

Mr. PAUL. Thank you.

Senator BAUCUS. The hearing is adjourned.

[Whereupon, at 3:50 p.m., the subcommittee recessed, to reconvene at 9:41 a.m., Monday, April 23, 1990, in room SH-216, Hart Senate Office Building.]

PREPARATION FOR THE 1990 FARM BILL

Cost of Production

MONDAY, APRIL 23, 1990

U.S. SENATE,
SUBCOMMITTEE ON AGRICULTURAL PRODUCTION AND
STABILIZATION OF PRICES OF THE
COMMITTEE ON AGRICULTURE, NUTRITION, AND FORESTRY,
Washington, DC.

The subcommittee met, pursuant to notice, at 9:41 a.m., in room SH-216, Hart Senate Office Building, Hon. David H. Pryor (chairman of the subcommittee) presiding.

Present or submitting a statement: Senators Pryor and Baucus.

STATEMENT OF HON. DAVID H. PRYOR, A U.S. SENATOR FROM ARKANSAS

Senator PRYOR. Ladies and gentlemen, good morning. We welcome you this morning to this meeting. We are not even going to call this a hearing; this is going to be a meeting, more resembling, I guess you would say, sort of an old-fashioned town meeting. Many times in the Senate and in the House we hear from USDA and people from agencies and departments and statistics and facts and figures and bureaucracies and whatever.

But today, in this particular hearing, or meeting, I should say, we are going to hear from the farmers out there themselves. We are going to hear what they are having to say about not only what is going on in agriculture but more specifically the cost of production in American agriculture today.

This does, I might say, amount to or equate to the final meeting of the Subcommittee on Agricultural Production and Stabilization of Prices during the 1990 farm bill debate. And I would say that arguably this could be the most important.

Thus far this year, we have received testimony from representatives of a wide range of commodities, each offering suggestions in their specific areas. The issue of today's hearing is a little different. It is one shared by all farmers, all farmers alike, the problem cutting across commodity lines and regional boundaries alike. Today we are to receive testimony and discussion from a variety of farmers from across the country on the cost of production, what it takes to get food from the field to our plate.

Unfortunately, the importance of that vital transfer of food from the farm to the grocery store is one that very few in our country appreciate. Even fewer Americans recognize the essential role of the Federal farm programs which enable the producer in America to provide us with the safest and most bountiful supply of food in the world.

The American consumer may hear a great deal about the cost of farm programs. That is constantly in the news. Yet there is very little or no recognition of the real obstacles a farmer faces in producing that crop. I sincerely hope the day does not arrive when consumers discover the cost of *not* having Federal farm programs! It would be a tremendous economic impact on the American consumer of food.

With the continuing rise in the cost of production and a further reduction in Federal farm outlays, the very real possibility exists that farmers will find themselves once again, as in the early 1980's, with their backs against the wall. If that day comes, and it may well, people will finally realize that Federal farm programs subsidize the consumer much more than the farmer.

As some of you have noticed from the displays around the room today, the cost of production for our Nation's farmers has been on the rise during this past decade. The American farmer is well aware of this problem. He and she sense it. They see it every day, rising prices for just about everything. Also, the local banker sees it. Yet it is a fact that many of the public fail to recognize. Climbing this tall ladder of cost increases, facing adverse weather conditions, uncertain agriculture programs, we are all trying to deal with the uncertainties of the potential results of the GATT negotiations the administration is participating in overseas, making planting and business decision very, very challenging for the farmer.

Yet here in the United States we continue to enjoy the most affordable food and fiber prices in the world. True enough, food prices have risen, but that is not reflected in the farmer's pocketbook.

If we are to keep the American farm family viable, not only as an efficient source of food and fiber for the consumer, but as an economic force in the local community, we must ensure that the Federal Government will do all it can to assist in securing and protecting export markets and providing a meaningful safety net that will enable the farmer to survive in the face of consistent rises in the cost of production.

Just a few facts to open this morning:

Each year the American farmer pays about $4.6 billion in real estate taxes, $600 million in personal property taxes, $3.8 billion in Federal and State income taxes, $350 million in sales taxes;

In the past decade, wages for farm workers have increased over 100 percent. Cost of tractors and equipment have increased by 200 percent.

The impact on agriculture in America:

One, agriculture is today America's largest single employer. There are over 2 million farmers in the United States. Agriculture requires the services of more than 20 million people to store, transport, process, and merchandise these farm products. Farm use of steel accounts for 4,000 jobs in the steel industry alone. Farmers use more kilowatt-hours of electricity than the entire residential use of all of New England and the District of Columbia combined. Agriculture purchased enough rubber products last year to put tires on more than 5 million automobiles. To reach consumers, our food had to travel over 174,000 miles on railroads. And today 1 hour of farm labor produces 17 times as much food and fiber as it did in 1919 to 1921.

These are a few facts and figures and concerns to lay out before our meeting begins this morning. Once again, we are going to hear informally from real farmers who face the day-to-day cost of production increases.

Our first witness happens to be a very fine friend and farmer from Lonoke, Arkansas, Mr. John Tull. Mr. Tull is a well-known rice farmer in this area of our State.

Mr. Tull, we welcome you, and please, if you would, just take the center microphone and, as we say, tell it like it is. Thank you.

STATEMENT OF JOHN TULL, RICE FARMER, LONOKE, AR

Mr. TULL. Thank you, Senator.

Senator PRYOR. Mr. Tull, let me note before we begin, this morning the U.S. Department of Agriculture—they are not on our list of witnesses—they have asked that they be allowed to come forward and make a statement. We have granted this, and at some time during the meeting, probably after the first two or three witnesses, we will probably call on USDA and see what they have to say.

Mr. Tull, we appreciate you.

INTRODUCTION

Mr. TULL. Thank you, sir. Good morning. My name is John Tull, and I own and operate a diversified rice farm in Lonoke, Arkansas. Our principal crop is rice, and that specifically is what I would like to talk to you about today. I have been growing rice on the same farm essentially all of my life with the exception of my school years and military service.

Production costs have increased every year that I can remember, while the price of rice has been relatively stable, with only slight increases. We have been able to stay in business only by increased yields, which have made us more efficient but at a higher cost.

FIGURES AS AN EXAMPLE OF MY PREVIOUS REMARKS

I would like to cite a few figures as an example of my previous remarks. The cost data is from the University of Arkansas Extension Service and the Economic Research Service of the USDA here in Washington.

The Arkansas extension data includes only variable cash production costs, and no land ownership or rental costs. Since the USDA data does include land costs, I will add them to our Arkansas data to make them more comparable.

I realize that given enough leeway, one can prove anything with figures, but I have made an honest effort to combine data from different sources to prove a point important to farmers.

Arkansas, as you may or may not know, is the largest rice producing State in the United States and has probably the lowest production costs for rice. Production costs are always the loser and vary greatly with the farmer, soil type, variety grown, and the water supply.

Personally, I have always had trouble with the Arkansas Extension Service figures, as I think they reflect only minimal inputs. Historically, production costs and returns seem to follow a pattern. Let's look at a few of these combined figures and see what they show us.

In my historical trend figures I have used Arkansas data for variable cost and yield and the average price is the USDA average for the United States for the year. The result in income or loss figure is their combination with the customary rent taken out of one-quarter of gross sales as the land cost.

In the year 1976, our variable costs in Arkansas were $214.70 an acre. Our average yield was 4,230 pounds. Our average U.S. price was $7.02 a hundredweight. This brought us a net return of $63.97 per acre.

In 1980, our costs were $272.06 per acre. Our yield, 4,413 pounds. Our average price, a whopping $12.80 an acre. This brought us a return of $133.45 per acre.

In 1985, our variable costs had increased to $374.84; our average yield, 5,200 pounds; our average U.S. price was $6.53 a hundred. That brought us a net loss of $120.17 per acre.

In 1989, preliminary figures show us that our variable costs were $340.20 per acre. Our average yield was 5,600 pounds. The average U.S. price was $7.24 a hundredweight—for a net loss of $42 an acre.

I think that these figures bear out my comments on the relationship of escalating costs and yields and lower prices and their relationship to total return. I picked some of the good years and some of the bad years. The preliminary 1989 figures I do have a problem with. But increased yields and prices certainly have made a difference.

I may have failed to mention that these figures do not reflect any income from Government programs.

To dramatically illustrate an example of increased costs, I picked some toy farm implements.

Pardon me, Senator.

This is a state-of-the-art—that goes on here—rice combine, similar to what we used in Arkansas. It doesn't make any difference whether it's green or it's red, I think we have the same effect. Today this state-of-the-art rice combine without the header costs $105,600. The slightly smaller model combine in 1989 cost $75,000. And the state-of-the-art model in 1978 cost us $35,000.

This medium-size tractor, similar to what we use, today costs $54,900. This same tractor in 1988 cost $52,400. And in 1977 it cost $22,450.

The efficiency of these implements has increased our production along with their cost, but not to that extent. The cost of operation of these implements has escalated along with the purchase price, these being the fuel, the tires, repairs and maintenance, insurance, interest, property taxes and also the labor to drive them.

While rice in 1978 was worth $8.16 a hundredweight, in 1989 it was worth only $7.24, on the average. And we no longer had the benefit of investment credit.

All of these examples I have used only tell me one thing, and that is: Because of increased costs and flat prices, the only thing keeping us in business is increased yields; and they have about reached their agronomic maximums. It is obvious that we cannot continue to farm without help.

WE CANNOT CONTINUE TO FARM WITHOUT HELP

To illustrate, I would like to use a March 1990 study recently released by the ERS, and this study is based on the 1988 crop and is the latest data available.

This study uses all the information previously used and then compares it to the added production costs and returns with Government programs, both deficiency payments and marketing loan benefits to the farmer. Without Government programs, for the year 1988 our costs were $450.91 in Arkansas, and in the United States the average cost was $475.14. The average return to the Arkansas farmer was $85.57 net loss per acre. The U.S. returns were $104.81 net loss per acre.

Let's look at it with Government programs, that necessary help.

Now, with Government help, in 1988 there was a $526.60 cost to the Arkansas farmer. I might add that most folks don't realize that with set-asides, working the set-aside land, loss of income, to conform with the Government program, that we have increased costs, Senator, when we have to conform to the Government program.

The U.S. average cost was $547.16 per acre. With the Government programs, that is, both deficiency payments and marketing loan payments, the Arkansas farmer returned a $52.22 net gain for his management and risk. In the United States the average gain was $48.55 per acre.

I might add that this looks pretty good, but when you look at it from another perspective, I think that the average farm, rice farm, in Arkansas is probably about 1,000 acres; the average rice crop in Arkansas after set-aside is probably 300 acres—and this may be a bit above average; so at $50 an acre—and I have 300 acres of rice—that looks to me like I made $15,000. My tractor drivers make $15,000 a year. So I don't think this is any great boon. Certainly it's necessary and we appreciate it, but in no way does it make us rich, folks.

This does illustrate the necessity for help in the form of target prices and marketing loan program in rice. The 1990 projections our guess is, since we haven't planted a crop yet—it's too wet—are the operating costs for Arkansas of $337.99 per acre, yields of 5,400 pounds per acre at a price of $7 a hundredweight. Taking out rent, this gives us a net loss of $54.49 per acre. If we were to add the Government programs less Gramm-Rudman, I think that we would come out similar, perhaps less, than in 1988. We simply cannot afford any cuts in target prices without lowering of production costs.

CONCLUSION

Somehow, some way, the message needs to be gotten across that if we in these United States want to continue to enjoy abundant and healthy food at the cost of the lowest percentage of disposable income in the world, then we are going to have to help the poor guy out there growing it. We simply, with all of our state-of-the-art equipment, increased yields, and technology, cannot compete with the outside world of no rules and rewards. The American dream is not mere subsistence but a reward in life commensurate with our effort.

Thank you, sir.

Senator PRYOR. Thank you, Mr. Tull.

If I could, let me ask two or three follow-on questions here. I think this would be the appropriate time rather than have all of our witnesses go through their testimony.

Let me first announce that immediately following our meeting this morning we are going to have a nice luncheon served to all the participants and to the audience, and we are going to try to demonstrate exactly what the farmer gets from those particular items on the menu. We think it's pretty dramatic, and we would appreciate, and certainly extend an invitation to you, Mr. Tull, and to all the participants and witnesses plus the members of our audience today.

What do you think has been the largest single contributor to the increasing cost of production for you, let's just say for the last 10 years? What has been the largest single cost increase?

Mr. TULL. Energy, sir. And it is related.

Senator PRYOR. Energy costs?

Mr. TULL. And its related items such as chemicals, which are primarily petrochemicals. Yes, sir.

Senator PRYOR. Very few people who are not in the rice producing States realize the cost of energy in having to irrigate and to bring the water to the rice. Now, is there a cost per acre for this that you could determine?

Mr. TULL. Well, Senator, of course that varies with the water table and varies with the power. But I am going to say $40 to $50 an acre, as a rough guess. I think that's what my costs are.

Senator PRYOR. Mr. Tull, let me ask this. There is some discussion—in fact, it has been proposed—a so-called income means test. What would this mean to the average rice farmer in, let's say, the State of Arkansas or the other four producing rice States?

Mr. TULL. I'm sorry, sir, I don't understand "income means."

Senator PRYOR. There is an income means test that has been discussed in the committee and actually I would say sort of proposed by the administration. And that would mean that every farmer and every farm owner would have to basically submit themselves to an income means test. If they had an income over a certain average, then they may not be ruled eligible to participate in Federal programs.

What does that mean to us down in Arkansas?

Mr. TULL. I understand your question now. I'm sorry, sir.

I don't think it would personally, if I understand the maximums, affect me personally. It would a lot of folks. But that is really not the point, Senator. The point is that why should we in these United States put a cap on our incentive to perform and do the best job that we can? Certainly we want to make the highest income for ourselves and our family we can. And I just don't see putting a cap on it, sir.

Senator PRYOR. We are pleased this morning to be joined by Senator Baucus of Montana.

Max, just a few moments ago, Mr. Tull, who is from Arkansas and a rice farmer, held up some tractors and other equipment showing the cost, the increase in cost, since 1980.

I wonder if you would do that quickly again for Senator Baucus. He may not know what we're faced with down there.

Mr. TULL. Well, first, Senator, these are just medium-size tractors. They may be a bit large for a livestock operation. But for rice, they're just medium size. This, I must say, has air-conditioning, radios, but you can't buy them without that anymore. [Laughter.]

This is the state-of-the-art tractor. It's green. It's just like the red one over there. And this tractor today costs $54,900. In 1977 it cost $22,450, a comparable size.

The combine that I have at my feet is over $100,000, and I think you can figure out these net losses per acre, how many years it would take to pay for that combine, sir.

Senator PRYOR. Thank you, John.

Senator BAUCUS. Well, Mr. Tull, I want you to know that you have no stronger advocate for rice farmers than the Senator from Arkansas. He and I were in Europe a year ago, trying to persuade the European Economic Community to be reasonable.

Mr. TULL. With their levy, yes, sir.

Senator BAUCUS. Yes. And open up a little bit. And whenever we would meet with various groups, including the Prime Minister of England, the Prime Minister of France, or the President of the Economic Community, Senator Pryor let them know what they should be doing, very, very effectively. I want you to know that he did a terrific job.

Senator PRYOR. In fact, I made the speech so often in each country, I think my colleagues became pretty bored. When I would start, they would leave the room. I knew I was kind of overstaying my welcome.

Senator BAUCUS. It was really a one-two punch. Senator Pryor would talk on rice and I talked about the beef hormone ban. They knew we were there. [Laughter.]

Mr. TULL. Senator, I know you only by reputation. I do appreciate your concern for all of us. And I do grow beef cattle in my diversified farm.

Senator BAUCUS. That's terrific. Good.

Thank you.

Senator PRYOR. John, thank you.

We are going to allow some witnesses to come forward in a moment. First, we are going to call on Senator Baucus to see if he might have an opening statement or any comments.

STATEMENT OF HON. MAX BAUCUS, A U.S. SENATOR FROM MONTANA

Senator BAUCUS. Thank you, Mr. Chairman, for holding this hearing today on the critical use of increasing costs of production.

In preparing for markup of the 1990 farm bill, this committee has held several dozen hearings and heard testimony from every sector of the farm economy over the past year.

I personally have spent many hours talking to Montana farmers and ranchers about their concerns in the farm bill.

One message has come through loud and clear.

We must put an end to the steady decline of net farm income.

I know the Bush administration officials claim that farm income is high.

But the fact of the matter is that, in real terms, farm income during the 1980's was the lowest it has ever been since we started keeping records in 1910.

During the 1910's, net farm income was $51 billion; in the 1930's it was $31 billion; in the 1950's, farmers made about $48 billion; in the 1970's they made $41 billion; and during the 1980's they made only $29 billion.

We, in this committee, must work to turn this situation around for farmers.

One of the reasons farm income has been on the decline is that target prices have been going down and farmers costs have been going up.

If we continue this pattern, we will soon have a mass exodus of farmers from their land.

That is why I recently introduced legislation that will tie adjustments in target prices to an index of farm input costs.[22]

This indexing would both rise and fall depending on the input costs of farmers. That way farmers will know that they will be working under the same relationship of return-and-cost as they will be when the 1990 farm bill passes.

According to statistics compiled by the Food and Agricultural Policy Research Institute (FAPRI) at the University of Missouri, the cost of production on wheat rose from $56 per acre in 1986 to $65 in 1989. The cost of producing oats over that same period rose from $50 per acre to $60; barley rose from $58 to $66; and the yearly cost of producing a steer rose from $309 to $373.

FAPRI estimates that by the year 1999, the cost of producing wheat will increase by 63 percent; oats will increase by 62 percent; barley by 64 percent; and the yearly cost of producing a steer will increase by 6 percent.

Clearly, farmers will not be able to withstand these cost increases.

This committee must address this issue in this farm bill.

I look forward to your testimony.

Senator PRYOR. Fine.

We are going to go to Billy Griggs, who is a peanut farmer from—now how do I pronounce that?

Mr. GRIGGS. Dooly County, Georgia.

Senator PRYOR. Dooly County. All right. And what is the name of that community?

Mr. GRIGGS. Unadilla.

Senator PRYOR. Unadilla, Georgia. I have never heard of Unadilla. What size is Unadilla?

Mr. GRIGGS. We have about 2,000 population there.

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[22] S. 2336, to amend the Agricultural Act of 1949 to provide for target price adjustments for the 1991 through 1995 program crops based on an index of production costs of farmers, and for other purposes. Some provisions included in S. 2830, Food, Agriculture, Conservation, and Trade Act of 1990.

Senator **Pryor**. Very good. Well, we appreciate your being here this morning.

Mr. **Griggs**. Thank you, sir.

Senator **Pryor**. Thank you.

Senator **Baucus**. What part of Georgia is that?

Mr. **Griggs**. That's in middle Georgia. I am on the northern fringes of the peanut belt within our State. We grow cotton, peanuts, soybeans, some beef cattle, and wheat. That's our main crops.

Senator **Baucus**. Thank you.

Senator **Pryor**. Billy, before you start, I want just to have a little add-on to what Mr. Tull said about you couldn't buy one of these tractors now without air-conditioning and a radio. Years and years ago, my father was the local Chevrolet dealer in our hometown, and I can remember very well when a car came equipped without a heater and without a radio and you had to sign up and order a heater on your car in advance, and a radio on your car. And now of course it's standard. So I guess the manufacturers of the tractors and all that equipment are making that standard equipment on theirs. But at any rate, that's probably not what runs the price up so much.

But we appreciate you, Billy, being here this morning.

STATEMENT OF BILLY GRIGGS, PEANUT FARMER, UNADILLA, GA

Mr. **Griggs**. Thank you, sir. I certainly understand his comments about the tractors and the costs of those. We are very familiar with those in Dooly County also.

INTRODUCTION

Mr. Chairman, my name is Billy Griggs. I am a farmer from Dooly County, Georgia, and I am speaking here today on behalf of the peanut farmers with the Georgia Peanut Commission. Our commission represents some 11,000 peanut farmers who account for about 46 percent of the peanut production in our Nation.

We wish to commend you, Mr. Chairman, and the members of the subcommittee for holding this very important and timely hearing on agricultural costs.

THE COST OF PRODUCING PEANUTS IN GEORGIA AND THE NATION HAS INCREASED SIGNIFICANTLY OVER THE PAST DECADE AND A HALF

The cost of producing peanuts in Georgia and the Nation has increased significantly over the past decade and a half. In 1975, according to data developed by the University of Georgia Cooperative Extension Service, the average per acre cost of producing peanuts in Georgia was $332.

This is indicated on our chart[23] over here on my right. The black line begins in 1975 and proceeds over to 1990.

This year, the Extension Service estimates that the per acre cost will be $655. This is an increase of 97 percent, which is almost double, in 15 years.

The significant line on this particular chart is the red line, which represents the trend.

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[23] See p. 457 for Chart 1—Georgia Average Cost Per Acre (Peanuts).

The overall cost has been virtually across the board for all inputs necessary for the production of peanuts. The most persistent increases have occurred in cost to the farmers of fuel, pesticides, fertilizers, seed, equipment, and labor. By their very nature, these inputs are almost certain to continue to rise in the future—some of these perhaps drastically.

While the per acre cost of producing peanuts has increased steadily, per acre yield of peanuts has trended downward over the same period. In 1975, according to the Extension Service, the per acre yield in Georgia was 3,295 pounds. Last year, the per acre yield was only 2,700 pounds, a decline of 18 percent since 1975 (see chart 2, p. 458).

Again, going to the middle chart here, the black line represents the yield per acre. The significant line in that again is the red line, the trend line, the downward trend.

The reasons for this disturbing downward trend in yields are less easy to identify than the increase in per acre production costs. Several factors that we know contribute to this trend are adverse weather cycles, loss of necessary production chemicals due to public perception of hazards, EPA actions, and the decline in basic and applied agricultural research related to peanuts due to the level funding patterns of agricultural research in recent years.

CONCERN OF PEANUT FARMERS

Peanut farmers in our State, and indeed the Nation, are concerned that this downward trend in yields will at worst continue and at best cast an uncertainty over their future. This concern is currently exemplified by the outbreak in Georgia and throughout the Southeast of a new plant disease called tomato spotted wilt virus that affects a number of crops, including peanuts. This virus, which appeared significantly for the first time last year, has reduced yields by up to 65 percent on farms where it has been identified. To date, no satisfactory method of controlling this disease has been found.

Mr. Chairman, it is obvious that these two distinct trends in peanuts—increasing production cots and declining yields—are having a severe impact on the farmers' per pound production cost. Per unit costs, of course, increase in inverse proportion to yields. Again, using Extension Service statistics for Georgia, the average cost of producing a pound of peanuts has increased from 10.1 cents in 1975 to 23.8 cents in 1989 (see chart 3, p. 459).

This is indicated in our chart on the far right, and the black line represents the cost. But the significant point is the red line, the trend, and it is at a greater increase than either of the other two.

That is an increase of 136 percent in the per pound production cost in 15 years, a far sharper increase than is reflected in the rise in per acre production cost. You can readily see, Mr. Chairman, how the peanut farmer's net income is being squeezed from both sides.

We again commend the subcommittee for holding this hearing and appreciate the opportunity of appearing before you. I will be pleased to respond to any questions you may have.

[The prepared statement and charts 1-3 of Mr. Griggs follow:]

STATEMENT OF BILLY GRIGGS TO THE SENATE SUBCOMMITTEE ON AGRICULTURAL PRODUCTION AND STABILIZATION OF PRICES ON COST OF PRODUCTION OF PEANUTS IN GEORGIA MONDAY, APRIL 23, 1990.

Mr. Chairman, my name is Billy Griggs. I am a farmer from Dooly County, Georgia, and am speaking here today on behalf of the Georgia Peanut Commission. Our Commission represents some 11,000 peanut farmers who account for about 46 percent of the nation's annual peanut production. We wish to commend you, Mr. Chairman, and members of the Subcommittee for holding this very important and timely hearing on agricultural costs.

The cost of producing peanuts in Georgia and the nation has increased significantly over the past decade and a half. In 1975, according to data developed by the University of Georgia Cooperative Extension Service, the average per acre cost of producing peanuts in Georgia was $332. This year, the Extension Service estimates that the per acre cost will be $655. This is an increase of 97 percent, almost double over 15 years (see Chart 1).

The overall increase has been virtually across the board for all inputs necessary for the production of peanuts. The most persistent increases have occurred in cost to the farmers of fuel, pesticides, fertilizer, seed, equipment and labor. By their very nature these inputs are almost certain to continue to rise in the future - - some of these perhaps drastically.

While the per acre cost of producing peanuts has increased steadily, per acre yield of peanuts has trended downward over the same period. In 1975, according to the Extension Service, the per acre yield in Georgia was 3295 lbs. Last year, the per acre yield was only 2700 lbs., a decline of 18 percent since 1975 (see Chart 2).

The reasons for this disturbing downward trend in yields are less easy to identify than the increase in per acre production costs. Several factors that we know contribute to this trend are adverse weather cycles, loss of necessary production chemicals due to public perception of hazards, EPA actions, and a decline in basic and applied agricultural research related to peanuts due to the level funding patterns of agricultural research in recent years.

Peanut farmers in our state, and indeed the nation, are concerned that this downward trend in yields will at worst continue and at best cast uncertainty over their future. This concern is currently exemplified by the outbreak in Georgia and throughout the Southeast of a new plant disease called Tomato Spotted Wilt Virus that affects a number of crops including peanuts. This virus, which appeared significantly for the first time last year, has reduced yields by up to 65 percent on farms where it has been identified. To date no satisfactory method of controlling this disease has been found.

Mr. Chairman, it is obvious that these two distinct trends in peanuts - - increasing production costs and declining yields - - are having a severe impact on the farmer's per pound production cost. Per unit costs, of course, increase in inverse proportion to yields. Again using Extension Service statistics for Georgia, the average cost of producing a pound of peanuts has increased from 10.1 cents in 1975 to 23.8 cents in 1989. That is an increase of 136 percent in the per pound production cost in 15 years, a far sharper increase than is reflected in the rise in per acre production cost (see Chart 3). You can readily see, Mr. Chairman, how the peanut farmers net income is being squeezed from both sides.

We again commend the Subcommittee for holding this hearing and appreciate the opportunity of appearing before you. I will be pleased to respond to any questions.

GEORGIA AVERAGE COST PER ACRE
(PEANUTS)

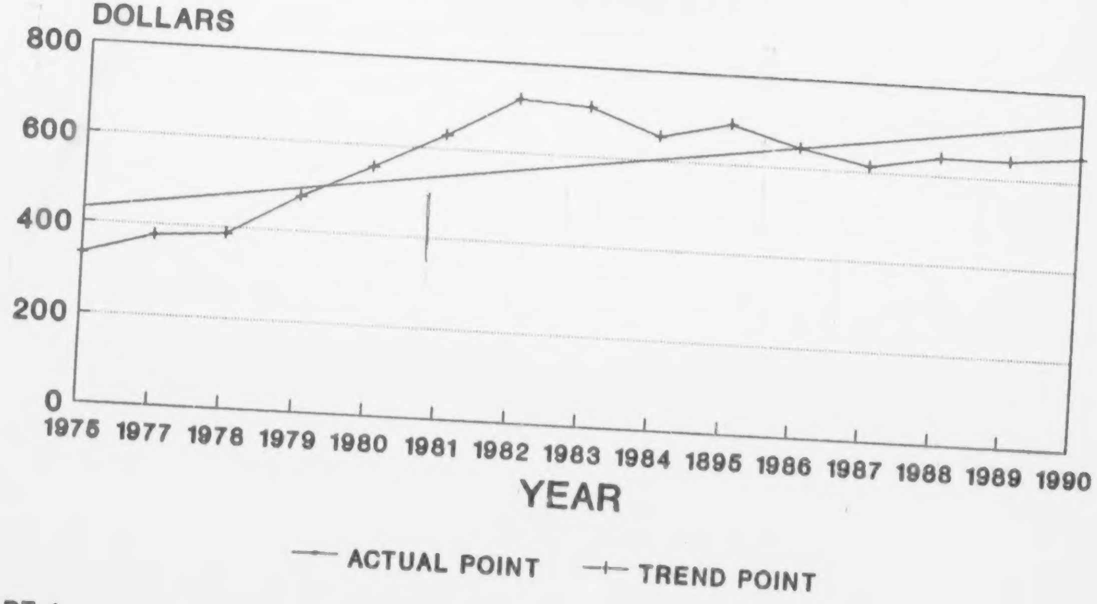


CHART 1

GEORGIA YIELD PER ACRE
(PEANUTS)

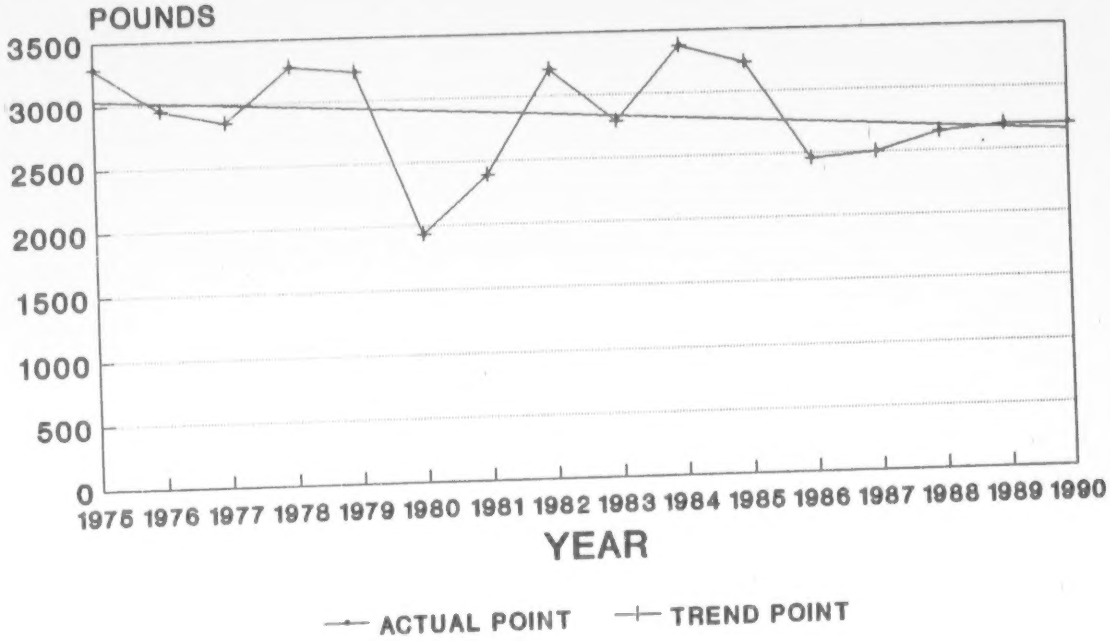


CHART 2

GEORGIA AVERAGE COST PER POUND (PEANUTS)

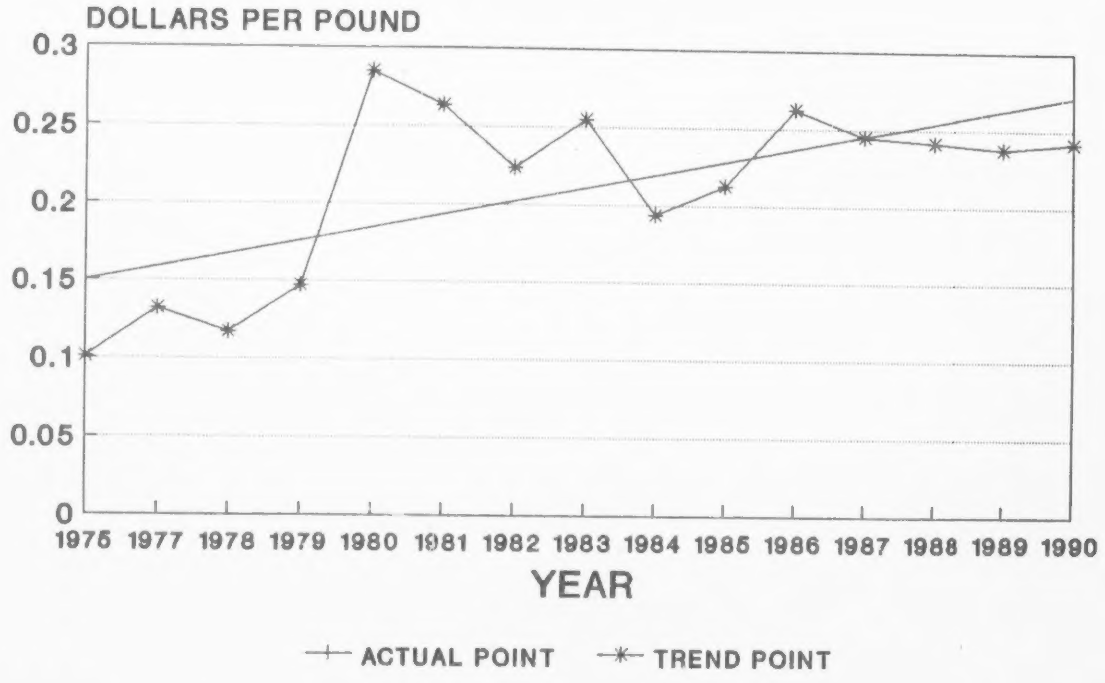


Chart 3

Senator PRYOR. Billy, what about interest rates for, let's say, the average peanut farmer there, are you seeing interest rates affecting the cost of production?

Mr. GRIGGS. It certainly has. In that 15-year period, we have gone through an inflationary rate in which it increased significantly, and then of course it has turned back down some. But the interest rates today are much, much higher than they were in 1975 and prior years.

Senator PRYOR. One of the big debates in the 1990 farm bill has been, and will continue to be, the issue of herbicides, pesticides, et cetera. What change have you seen in the last few years in the peanut crops with relation to this issue?

Mr. GRIGGS. Well, each time one of our tried-and-proven chemicals are removed from the market, then it brings on—in many cases—it brings on a reduced controlling effect on the disease or the weed, if that's what we're after in the herbicide. It brings on a reduced effect to that, a less efficient control of either the disease or the weeds that we're trying to control.

At the same time, the replacement chemical may cost much more per acre than the standby did at that particular time. Again, you get into, in the farmer's mind, you get into the perception of this particular issue, whether the chemical is in fact unsafe or whether it's the perception of it being unsafe.

But either way, it is a problem with us. We are losing our proven chemicals, and it is affecting our cost.

Senator PRYOR. What, to the best of your knowledge, is the single highest contributing factor to the cost of production increase?

Mr. GRIGGS. I would have to agree with Mr. Tull in his position in Arkansas with rice. Fuel has been one of our major increased costs. Peanuts, in the State of Georgia, we are approximately 60 percent irrigated. We share the benefit of having one of the highest quality peanuts in the world right here in the United States, and we in Georgia feel like—and perhaps we are a little bit biased—but we feel like ours is some of the best. But we do that through irrigated acreage and through proper management to our crops.

The fuel costs for our tractors, our combines, and our irrigation systems have had a tremendous impact on us.

Senator PRYOR. There was a story yesterday, I believe, or over the weekend, in the Washington Post, which were sort of looked at in the future years on oil prices and the long-term outlook, I think, and for the remainder of this century, for the next 10 years, is a steady, gradual increase as well as a growing dependence on Arab OPEC members for our oil supply.

What about this issue and the petroleum-based inputs to peanut production, does this relate?

Mr. GRIGGS. It certainly does. It leaves us with a little uncertain feeling there about what's coming in the future. As our dependency increases on OPEC and foreign oils, our prices will increase and our risk in production of our country, in feeding our Nation, increase greatly. We are concerned that this may come back to haunt us at some point in time.

We as farmers, and I feel that the Nation, the people in this Nation, want the United States to maintain a production level that is at least adequate to feeding our country and our people without inputs from other countries. I think that is a very basic need we have in the United States.

Senator PRYOR. Billy, we don't have a lot of peanut farmers in Arkansas. We have a few, but not many. Do most of the peanut farmers, say, in Georgia, in the program, are they also in agriculture in other crops?

Mr. GRIGGS. Certainly so. One of my main crops is cotton. I have some beef cattle on my farm, and I grow cotton. And in fact I am in the cotton business in warehousing and ginning with the family business. But there is very few just-peanut farmers. We are farmers that grow peanuts in our operation. But as I said, we have farmers that grow soybeans, wheat, corn, little bit of corn in our area, cotton. We are diversified in that section. Peanuts is a part of our production, but it is a vital part.

Senator PRYOR. Well, with the looks of the cost per acre increase, which is dramatic, and the yield per acre because of weather conditions or what have you, and then the cost per pound received by the farmers seems to be flat, it seems like the peanut farmer has to be involved in other area of agriculture to survive.

Mr. GRIGGS. Certainly so.

Senator PRYOR. Billy, we want to thank you for coming. Senator Fowler is very sorry that he could not be here with us. He is a very fine and able member of this committee. It is hopeful that Senator Fowler might be here a little later in the hearing. But we are very sorry he could not be here. He sent his regards over to you, and I am hoping he is going to be here with us this morning before we conclude. Usually Senator Fowler is known to at least show up when they start eating. [Laughter.]

So you stick around, and when they start serving I am sure he will be here.

Mr. GRIGGS. Well, I appreciate your regard for Senator Fowler, and we certainly share that.

Senator PRYOR. He is a very fine member of this committee.

Mr. GRIGGS. We certainly share that, the farmers in Georgia, and we appreciate the opportunity.

Senator PRYOR. Thank you very much, Billy.

Billy, later on, and all of our witnesses, after we complete our whole list of witnesses this morning, we may call on you to come back again if you want to say something else or if you want to sum up what you said earlier or compare your notes with some of the succeeding witnesses.

Mr. Jackie Theriot—am I pronouncing that right—a sugarcane farmer from Catahoula, Louisiana and the general manager of Breaux Bridge Sugar Cooperative, Inc. Breaux Bridge is a very famous place. We see a lot of publicity on Breaux Bridge, Jackie.

Mr. THERIOT. I hope it's good publicity.

Senator PRYOR. It is, and we appreciate your being here this morning.

STATEMENT OF JACKIE THERIOT, SUGARCANE FARMER, CATAHOULA, LA; TESTIFYING ON BEHALF OF THE AMERICAN SUGAR CANE LEAGUE OF THE U.S.A., INC., BREAUX BRIDGE, LA

Mr. THERIOT. Breaux Bridge is the crawfish capital of the world.

Senator PRYOR. I think that is undisputed.

Mr. THERIOT. Thank you, Mr. Chairman.

INTRODUCTION

My name is Jackie Theriot. I am sugarcane farmer from Catahoula, Louisiana, and the general manager of Breaux Bridge Sugar Cooperative, Inc., a processor of sugarcane into raw sugar. My experience with the production and processing of sugarcane includes volunteer work and two tours of duty with the Peace Corps in Africa, the Far East, and Central America. I am also a member of the board of directors of the American Sugar Cane League of the U.S.A., Inc., which is a trade association whose members include all 20 of the raw sugar processing mills in Louisiana and farmers who produce approximately 95 percent of the sugarcane grown in Louisiana. My testimony today is presented on behalf of the American Sugar Cane League. We appreciate this opportunity to present our views on the inclusion of cost of production increases in the 1990 farm bill.

WHILE OUR SUGAR INDUSTRY IS EFFICIENT, WE ALSO REQUIRE A LARGE INPUT COST PER ACRE

While our sugar industry is efficient, we also require a large input cost per acre. Sugarcane production is unlike other crops in that it is a multiyear crop—planted one year and reharvested annually for a number of years. It requires heavy investment in specialty equipment and labor from planting through harvesting, which is not the case for most program crops.

PRODUCTIVITY PER ACRE HAS STEADILY INCREASED

Productivity per acre has steadily increased due to numerous reasons, including improved germplasm, technologies and machinery, as well as excellent climatic conditions for the last three crops. The increase in total sugar yield has been primarily attributable to this increased productivity rather than increases in acreages planted to cane.

SUPPORT DATA ON PRODUCTION COSTS

Support data on production costs are based on data from the Louisiana State University Agricultural Economics and Agribusiness Department and the data from the Farm Credit System. These documented production costs have increased by 23.7 percent in real dollars during the period 1986 through 1989. During this same time, the loan rate for raw sugar has remained constant, as directed by the 1985 farm bill, which means a decline in the loan rate of 18 percent in real dollars. This disparity continues to increase and ONLY because of increased productivity on our part and favorable weather has this been allowed to survive to this date.

RECORDBREAKING FREEZE

In December of 1989 the State of Louisiana experienced a recordbreaking freeze which destroyed a very significant percentage of our sugarcane which was to be harvested in the fall of 1990. Although it is still too early to determine the actual damage which resulted from that freeze, current estimates indicate that between 40 and 60 percent of our 1990 crop has been destroyed. Because sugarcane is not grown from seed, as are other crops, but from planted stalks of cane, the destruction of that cane due to the December freeze will greatly increase our cost of operation not only in 1990, 1991, but also probably in 1992.

LABOR COSTS

As you are aware, the Federal minimum wage was increased from $3.35 per hour to $3.80 per hour, effective April 1 of this year, and will further increase to $4.25 per hour on April 1, 1991. Although most Louisiana sugarcane field workers and sugar factory workers are paid wages in excess of the minimum, in all probability the increases in the minimum wage will result in an increase in the wages of employees who are presently paid more than the minimum.

POSSIBILITY EXISTS THAT THE PRICE OF OIL WILL SUBSTANTIALLY INCREASE DURING THE DURATION OF THE 1990 FARM BILL

In addition, the distinct possibility exists that the price of oil will substantially increase during the duration of the 1990 farm bill. If such an increase occurs, the price of fuel we must purchase for our equipment and machinery and the price of the chemicals and fertilizers to be applied to our crops will also increase substantially.

CONCLUSION

Mr. Chairman, to reiterate, we anticipate that our costs of production will increase significantly during the duration of the 1990 farm bill. Unless the bill provides us with cost-of-production increases, we will have no way of recouping those increased costs. That ability will certainly reduce our margin of profit and will further hinder us in our efforts to compete with heavily subsidized foreign-produced sugar. We, therefore, strongly urge that a cost-of-production increase be included in the bill.

Again, I appreciate the opportunity of testifying before you and would be happy to attempt to answer any questions you may have at this time.

Senator PRYOR. Thank you very much, Jack.

Let me ask about an issue that you did not raise, but having seen the sugarcane industry and watching production of that I was fascinated with it. Does the issue of wetlands ring a bell? Are you involved in this issue as a sugarcane farmer? What is the situation with the wetlands?

Mr. THERIOT. I would say, Senator, that 90 percent, maybe 95 percent of our sugarcane producing acreage in Louisiana is under the wetlands issue. And I know you people are diligently trying to overcome that situation today. But it was just a faux pas that occurred, and I feel that not only sugarcane farmers but most farmers who are involved in the wetlands issue, and in fact the business people of our area, will be concerned about this because of the liability imposed on that acreage.

Senator PRYOR. What is the present status with the wetlands issue? What are farmers doing right now to cope with the present law and the present regulations issued by the various agencies?

Mr. THERIOT. At this time we are trying to follow the law to the "t" as far as applying for section 404 permits to the Corps of Engineers. However, we have lobbied strongly at the State level and also in Washington to try to get a redefinition of wetlands so that we can better live. We would like to have at least the wetlands that we have been farming for years; we would like to see that be grandfathered into the farming operations and not be involved in the section 404 permit.

Also, our rice farmers, of which we have quite a few in Louisiana, are involved because from what I understand, any levee that is over 24 inches high has to be permitted by the section 404.

Senator PRYOR. And sometimes there is a 60- to 90-day waiting period; is this correct?

Mr. THERIOT. Probably more than that, Senator. Sometimes I have heard permitting as long as 6 months. And it's impossible to live with that situation.

Senator PRYOR. What about just an exemption for normal agriculture practices or normal farm practices, do you think this would suffice?

Mr. THERIOT. I think this would certainly be a trend in the right direction. We are trying to get this acreage grandfathered in, and at the State level we are active now with the legislature in session and we are attempting to get that done. So, hopefully, we will have some relief in that area.

Senator PRYOR. I announced a couple of weeks ago that we are going to form sort of a wetlands caucus here in the Senate, trying to get the people who are interested in this issue. This is in no way an antienvironmental stance, this is a group of Senators, several from this committee, several who are not on this committee, Democrats and Republicans alike, seeking to make sense right now of a convoluted situation where the farmers do not know the rules and certainly none of us knows the ultimate results of what will happen.

So I hope you will go back home and tell them that we are very sensitive to this issue. We are going to try to take some action as soon as possible. And I think it will be very soon.

Mr. THERIOT. In fact, I might add that Mr. Soileau, who is the director of the wetlands in Louisiana, has indicated that this will delay their environmental concern of wetlands because of the situation with the farmers. He is very concerned about this.

Senator PRYOR. Good. Jack, we want to thank you for coming. And once again, after a while, when we complete our witness list, if there are things that you want to add, you will be invited back to the podium.

We very much appreciate your being here with us.

Mr. THERIOT. Thank you.

Senator PRYOR. Senator Breaux and Johnston recommended that you come up for this hearing, and I am sorry that they could not be here to personally welcome you.

Mr. THERIOT. I appreciate being here.

Senator PRYOR. Thank you very much.

Mr. **Theriot**. Thank you.

Senator **Pryor**. Now, because Senator Baucus has made this request, we are going to move Jim Wilson from Trout Creek, Montana, to the next slot on the program.

Is Mr. Wilson in our audience at this time? I don't know that we're going to move Mr. Wilson. He is not here, is he? Is he here?

Senator **Baucus**. Apparently he is not here yet.

Senator **Pryor**. Well, he may be in Trout Creek.

Senator **Baucus**. He may be in Trout Creek.

Senator **Pryor**. He may be still in Trout Creek.

But anyway, we will move on then.

Senator **Baucus**. Thank you.

Senator **Pryor**. Is that all right with you?

Senator **Baucus**. Fine. You bet. Thank you.

Senator **Pryor**. Where is Trout Creek, Montana?

Senator **Baucus**. Trout Creek, Montana, is up near Noxon, Montana.

Senator **Pryor**. Well, wherever it is, it sounds good.

Senator **Baucus**. It is also up near Thompson Falls, Montana.

Senator **Pryor**. Sounds like it'd be more fun to be there than Washington, D.C., right now.

Senator **Baucus**. It's near the Clark Fork of the Columbia in western Montana.

Senator **Pryor**. Well, we will be on the lookout for Mr. Wilson.

Senator **Baucus**. And he is actually near Hot Springs, Montana.

Senator **Pryor**. Hot Springs, Montana.

Senator **Baucus**. That's right.

Senator **Pryor**. Well, we next have on our regular order a cotton farmer from Lamesa, Texas, Mr. Lloyd Kline. I believe Mr. Kline is here.

Mr. Kline, we appreciate you being here. Thank you.

STATEMENT OF LLOYD KLINE, COTTON FARMER, LAMESA, TX

Mr. **Kline**. Thank you, Mr. Chairman. It's a pleasure to be here.

INTRODUCTION

I am Lloyd Kline, a cotton producer and a banker from Lamesa, Texas. That is in Dawson County, Texas. That's south of Lubbock in the high plains of Texas. And it might come as a surprise to you and to others here today that in the High Plains of Texas, where we have average rainfall of some 16 inches a year, that we do have wetland problems out there. It came as a surprise to us in the conservation compliance section of the law that we would have problems with the wetlands. We also have problems in the Playa Lakes.

Senator **Pryor**. You are a banker and a cotton farmer?

Mr. **Kline**. That's correct, sir.

Senator **Pryor**. Which is the hardest to perform right now, being a banker or a cotton farmer?

Mr. **Kline**. The last 10 years, both have been very hard. [Laughter.]

Senator **Pryor**. You have chosen two tough professions?

Mr. **Kline**. That's correct.

Senator **Pryor**. We look forward to your statement, Mr. Kline.

Mr. KLINE. We have three major crops in Dawson County, which is south of Lubbock, as I mentioned. We have cotton, we have cotton, and we have cotton. That's it. And so the cost in production of cotton has very strongly affected the High Plains of Texas.

AIR-CONDITIONING IN THE TRACTORS

I might add and tag on just a little bit to what was mentioned earlier about the air-conditioning in the tractors. One of our major costs in cotton production is equipment and labor when you a pay this price for equipment.

It used to be that you could go out and hire labor that couldn't get a job anywhere else, were not capable of working at any other profession or job, and put them on a tractor out on the farm and they could get by and make you a hand. No longer do you want to put that caliber of people on this high-priced equipment. And so, to compete with our neighbors in the city that provide air-conditioning and all the comforts in the offices that have labor hired in the cities, we must, in order to compete with those people, have the comforts that the office provides, out on the farm. And the only way to provide that is with air-conditioning, radio, and the comforts of the modern-day equipment.

WE ARE DISHEARTENED MANY TIMES WHEN WE READ AND HEAR OF UNINFORMED ATTACKS ON AMERICAN FARMERS

We are disheartened many times when we read and hear of uninformed attacks on American farmers who, because of the subsidization in foreign parts of the world, are required ourselves to have subsidization from the Federal Government in order to compete in world markets.

Many uninformed people in our great Nation today refer to the deficiency payments as profits to farmers. They have absolutely no appreciation or understanding of the kind of investment farmers have to risk to make a crop, particularly a cotton crop on the High Plains of Texas. They don't understand that the farmers are the most capital-intensive industry in America today.

COST OF PRODUCTION

Mr. Chairman, USDA reports that the national average cost of producing the 1988 cotton crop was $454 per acre, as reflected on the chart at the front of the room. That translates into 76 cents per pound. The target price for the 1988 crop was 75.9 cents a pound. I understand that USDA estimates that the cost of producing the 1990 crop at 80 cents per pound. The target price for the 1990 crop is 72.9 cents a pound.

The Southwest, which includes the High Plains of Texas, naturally, the 1988 cost of production was 75.5 cents per pound, very close to the national average. While our costs per acre are lower than the national average, so are our yields. Incidentally, they are also very variable and because of too much rain or too little rain, many times the High Plains is known for the disaster area of the cotton industry.

But in 1985 our cost of production in the Southwest was 70.42 cents a pound. The very next year was $1.05 a pound. So that shows you the variability of the cost in production in the High Plains of Texas of cotton.

SOME OF THE THINGS THAT ARE INVOLVED IN THE PRODUCTION FINANCING IN AGRICULTURE

Now let me switch and put on my banker's hat for a minute. Let me just briefly talk about some of the things that are involved in the production financing in agriculture, particularly cotton, which I am most familiar with.

Our bank is, and has been for years, totally dependent upon production and equipment loans and real estate loans in agriculture for our income. We looked, prior to the 1980's, primarily at collateral as the basis for our loans. In the late 1970's, early 1980's, we found ourselves in a position where no longer could we look at collateral when inflation stopped. I guess we were under the false impression that inflation would continue on and on. And so we began to look at cash-flow, which put a tremendous strain not only on banks but it also put a strain on producers. Probably we should have been looking more at cash-flow through the years.

However, as I look at the disastrous 1980's and primarily the early part of the 1980's, we began to turn attention to cash-flow. We took some substantial losses in the early 1980's in my bank and other banks across the High Plains and other agricultural banks across this great land and country of ours. We lost some 10 percent of our total loans that we had on the books as of January of 1981. We eventually lost those in write-offs. I now notice in the newspapers yesterday where FmHA write-offs are looking at where they were projected to be some $10 billion they now expect it to be $22 billion. The Farm Credit System, we are all aware of what took place in the Farm Credit System.

So what I am saying is that a great deal of the capital that was put into agriculture prior to the 1980's was not repaid. That's not going to happen again. Our bank, along with all other agricultural banks, are taking a very hard look at loan repayment ability of producers. It's going to be based on cash-flow.

That's going to be based on a couple of items. It's going to be based, first we look at target prices, what is the deficiency payment going to be, the average, the projected deficiency payments? It's very, very important in financing an operation. We look at the projected production income. We look at the loan basis for cotton. It all blends in to the cash-flow statement.

Then as a backup we look at Federal crop insurance, a very important part in the financing of agriculture. We look at it to see that if that disaster comes to our producers, which it does quite often one way or the other, we look at the backup on what does he have to be available to repay that loan.

So it is all blended together to make the producer's loan work, and if it doesn't work, he doesn't get financed. And if he doesn't get financed, he has to look for other means to be financed, either through FmHA, which is getting to be a rather difficult thing to have to do. And so it may mean that he is out of business.

I find that there is not a great deal of people wanting to go into agriculture now because of high risk and also because of the unavailability of capital. As I mentioned earlier, highly intensive requirement, high-risk capital, and not a great deal of people want to go into agriculture.

So we see our producers trending to be older and older and older, and it has just kept continuing. We have to get our younger people involved in agriculture.

THE BUDGET SITUATION

I can understand the budget situation. Being a banker, I can understand the problems that you have with the budget and how it will force Congress and others who help shape agriculture policy to make some very tough decisions. But I want to emphasize that in order to maintain an effective farm program, we must continue the target price at this level and make it on a sliding scale that would increase as production costs increase.

I THINK THE NATIONAL COTTON COUNCIL'S POLICY CONCERNING LOAN AND TARGET PRICES IS A REASONABLE APPROACH IN COTTON

I think the National Cotton Council's policy concerning loan and target prices is a reasonable approach in cotton. We favor continuing the current loan formula and we favor keying the target price to the cost of production, with the current 72.9 cents target price serving as the floor and escalating as the cost of production moves up, which naturally it will with the increased cost of labor in the future, increased cost of fuel in the future, increased cost of insurance in the future, increased cost of all the inputs, the chemicals that we use.

CHEMICALS ARE USED, AND THEY ARE USED VERY WISELY

And may I emphasize that in our area chemicals are used, and they are used very wisely and our people are very concerned about the environment and about contamination of underground water. And we are very careful with chemicals in our area.

But if the cost of producing the 1990 crop is 80 cents, as USDA estimates that I mentioned earlier, then the 72.9 cent proposed target price floor is well below the cost of production. I might add that the figures that I have used this morning are from USDA. The cost figures that local and State universities prepare many times differ, and there is some work being done now to put these two figures more in line with each other.

CONCLUSION

Again, Mr. Chairman, I want to thank you for the opportunity to be here. I commend you for holding these hearings, and it is absolutely necessary that to develop a sound farm policy and programs, that we continue on the same basis that we are and that we move forward with a target price deficiency payment that escalates as the cost of production moves up. Thank you.

Senator PRYOR. Mr. Kline, thank you very much.

I have always maintained, especially in the last few months, visiting with farm groups, that any farmer who has survived the last 10 years and is still farming is a true farmer. Now, I think we are seeing actually the survivors out there today that are still out there farming if they've survived this past decade.

Are you seeing that, as a banker, I would say?

Mr. **Kline**. I totally agree with you. Anyone who survived the disastrous 1980's are pretty strong-willed, and in most cases had quite a bit of financial strength and collateral behind them, in some cases, to dispose of and to raise capital to pay costs.

Senator **Pryor**. In your county in Texas, are there fewer farmers today than there were 10 years ago?

Mr. **Kline**. Yes. There may be a larger number of entities, but there are fewer farmers.

Senator **Pryor**. But there are fewer people out there on those farms?

Mr. **Kline**. That's correct. That's correct.

Senator **Pryor**. Well, I think that I have always used as a test that any of these programs and all of these programs, and when we talk about the farmer, I look at one thing, and that is: the net income. You can talk about selling more of this overseas and having greater exports and doing this, that and the other, and statistics. But somehow or another, that old net income is something that I think we have to look at, and this is one reason I think the target price concept is so absolutely essential to successful, meaningful farm program.

Mr. **Kline**. We absolutely have to have the target price system in order to maintain not only bottom-line profitability, net income, but we have to have it in order to continue financing these operations. And there are very few farmers across the United States that can finance themselves without borrowing money, and they must have a safety net to get financing.

Senator **Pryor**. As a banker, there is a proposal that we have talked about with Mr. Tull earlier, there is a proposal on an income means test for farmers. How does a banker look at an income means test in deciding whether or not a person gets a line of credit?

Mr. **Kline**. With a very jaundiced eye. The question that immediately comes to my mind when you talk about a means test, why penalize your most efficient operations? And I think if you look at the history of producers, the smaller, less efficient operations are the ones that have had to be bailed out through some backdoor kind of subsidization through FmHA and other means. So I think in the cotton industry you would be looking at probably half of the producers under a means test that would be affected. And certainly it would be much harder for that producer to be financed if he came in the category that the means test would affect him.

Senator **Pryor**. Senator Baucus.

Senator **Baucus**. I have one question, Mr. Kline. That is, what is the consequence of the cost of production continuing to go up disproportionate to farm income? Is it fewer cotton producers? I am trying to determine what the long-term consequences are both for family farmers, and for the degree to which the United States is a major producer. What are some of the longer-term implications?

Mr. **Kline**. Senator, the picture that I see, we must work in areas to increase the income to keep that from happening. And I think we're working that way in export markets as well as domestic markets. We in the cotton industry can continue to improve and have new varieties coming on that will continue to improve production, but there is a limit to increased and improved production offsetting the fact that you're not making a profit.

So what you have to do—and I think we're doing it and I think it will be done—is to continue to work toward getting more income. I don't think we will ever see the day that that really comes together that you have no profit in cotton. I think there will always be some profit there.

Senator BAUCUS. But what are the actual consequences? What does the future look like for the cotton industry if cost of production continues to rise without a proportionate rise in farm income?

Mr. KLINE. The next level that I would project would be corporate farming. That would increase costs to the consumer tremendously. Production would be based on, as in the automobile industry or the equipment industry, that if there's not a market for it, it won't be produced. And if you want this product, whether it be cotton or whether it be a food product, you're going to have to pay for it. And then if you pay for it, then corporate farming, large farming operations, would produce it for you.

But it would eliminate the family farmer as we know it today. That is out in the future, and I hope we never see it.

Senator BAUCUS. I very much agree. Your point, then, is that unless we can provide for adequate net income for enough producers, the result would be more large-scale corporate farming, and the consequence of that would be higher prices.

Mr. KLINE. Tremendous increase in the cost to the consumer.

Senator BAUCUS. So it's in the very direct interest of the consumers to be sure that there is sufficient net income for farmers so that we can avoid big increases in food and cotton prices.

Mr. KLINE. If you look at the numbers of people affected by the farm program, you find that consumers are more affected by the farm program than the producer. You have fewer producers—and after all, producers are consumers also—but the vast benefactors of the farm program are the consumers of this great United States.

Senator BAUCUS. Well, that is a point that we ought to do a better job of getting out. I don't think consumers fully understand that.

Mr. KLINE. I think you're correct, and we need to do a better job of it.

Senator BAUCUS. Thank you very much.

Mr. KLINE. Thank you.

Senator PRYOR. Mr. Kline, you made mention of some statistics and figures on cost of production which might be in dispute. And I noticed this in putting together this hearing. I don't know if Senator Baucus has had time to look at all the charts.

Senator BAUCUS. Yes, I did see those.

Senator PRYOR. I found something mysterious here, and we're going to talk to the USDA about it. Using their figures and statistics as an average between 1984 and 1986, we see a downward spiral of cost of production dollars. I don't know of one farmer in my State—maybe I assume not in Montana—that feels that they saw a decrease in the cost of production during those years.

Senator BAUCUS. I was going to ask that same question.

Senator PRYOR. I am sort of mystified. You have been in this business a long time. Did you experience that decrease in the cost of production at that time?

Mr. KLINE. If you look at it per acre, probably yes, sir, because—and I am not talking of myself, my operation, but I am talking about overall operations—money was tight, many people slacked off on fertilizers, they slacked off on chemicals, and the cost per acre may have decreased. But that does not necessarily trend to a cost-per-pound decrease.

Of course, weather has so many variable factors in it that you know, you can drop off fertilization for 1 or 2 years and get by with it. You have enough carryover built up in the land that you can make a reasonable crop, not your average yields, but a reasonable crop, on the carryover fertilizer. So you could say the cost of fertilizer, you may not keep the fields as clean, you may cut back on some labor costs. You can do that on a temporary basis, but a continuing basis, it would not be sustainable.

Senator PRYOR. They probably didn't buy a large number of tractors during that year.

Mr. KLINE. That's correct.

Senator PRYOR. They just fixed up their old ones.

Mr. KLINE. That's correct.

Senator PRYOR. As we say, put a little baling wire around them to keep them together.

Mr. KLINE. Sometimes you have to do that in times of short money supply availability.

Senator PRYOR. Mr. Kline, we appreciate this. By the way, I will say this to Mr. Kline, you are very knowledgeable on many of these issues and you come uniquely qualified as a banker and as a farmer.

We have told the press today who are covering our hearing that all of our witnesses during the lunch break maybe our witnesses will be available, and we hope that if some of the members of the media come and talk to you about firsthand experiences, that you and our other witnesses this morning will take part.

Mr. KLINE. Thank you, Mr. Chairman.

Senator PRYOR. Thank you.

Well, we understand now that Mr. Jim Wilson has gotten here from Trout Creek, Montana.

Mr. Wilson, we appreciate your coming. We are going to move you up to this next slot. Senator Baucus has requested this. We certainly appreciate your coming from such a long distance.

Senator BAUCUS. Mr. Chairman, before Jimmy begins, I would like you to know that Jimmy Wilson has been involved for many years in agricultural issues in the State of Montana as well as nationally. He has been very active with the National Cattlemen's Association, and I could think of no finer advocate for agriculture than Jimmy. I have known him for many, many years.

Senator PRYOR. Good.

Senator BAUCUS. He is very active, very involved, and all for the right reasons. He provides a very positive, constructive basis, educating not only all of us but also a lot of folks in my home State and around the country. He does a super job.

Senator PRYOR. Good. Thank you.

Senator **Baucus**. I might add he is one of my best friends, too.

Senator **Pryor**. Thank you.

STATEMENT OF JIMMY L. WILSON, CATTLE RANCHER, TROUT CREEK, MT

Mr. **Wilson**. Thank you very much, Senator Baucus.

INTRODUCTION

Mr. Chairman, for the record, my name is Jimmy L. Wilson, and I live in Trout Creek, Montana. Our operation consists of a cow-calf operation. We also background our feeder cattle. We raise small grains, and also we are in the timber business.

I would like to digress just briefly before we get into the subject at hand that we are in the week of celebrating Earth Day, and I want you to know the cattlemen have taken a large part in working toward a better environment and, hopefully, that all segments of agriculture will work in harmony with our environment because without a healthy environment we cannot continue to produce food at a wholesome rate that we have without taking care of the environment.

OUR COW/CALF OPERATION IS VERY INTENSE

This morning the steer that we are looking at here—and I am sure that everybody recognizes it as a steer; I hope it's a hereford. [Laughter.]

It weighs about 1,100 pounds. This is a finished steer that we're talking about. And you can see the percentages breaking down our costs on raising this animal.

Now, using our ranch as an example, we calve our cows starting March 1, and we raise these cattle on our operation. And I would suppose 80 percent of these calves in Montana and the West are shipped in the last part of October and November. However, to get more value added for our operation, we background our calves and sell them, usually in February, which traditionally in the last few years has given us a better marketing opportunity.

We also raise purebred cattle. We performance-test our bulls and our heifers as well as all of our commercial cattle. So our operation is a very intense operation.

WE OPERATE ON PRIVATE LANDS

We operate on private lands. Our operation consists of renting private land from our neighbors. Some of them unfortunately have had to sell their cattle herds because in Montana we have had 8 to 10 years of drought, and many of the people simply had to sell their cattle to hold their operations together.

We do not participate in any Government commodity program. Although we raise grain, we green-chop it for silage. So we are pretty much independent, and any decisions we make, if it's a wrong decision you only have one person to answer to, and that is our family operation.

My wife and I started this operation 30 years ago, and at the present time we have two of our boys that are involved as partners in the operation.

GRAIN AND SUPPLEMENT

Looking at the steer, the first segment that I would like to talk about is grain and supplement. And we are looking at 24 percent right along the top of the line on this steer. Now, our operation, as predominantly in most of the West, we raise grass hay. It's low on protein. Those people that can irrigate, we have an acidic soil and so we cannot raise alfalfa, we raise clover and hay. And so we do have to supplement the cowherd right before calving to give them enough protein so that they raise a good, healthy calf, and when the calf starts nursing the cow, why, it has a lot of milk.

So about 24 percent of the cost would be for grain and grain supplement. Now this is for our cow and also following this calf through as we background it and then as the calf goes into a feedlot back in the Midwest or in the Southwest, wherever the calves may go. About 24 percent of the total cost is for grain supplement. This also includes the mineral and protein that makes a balanced ration.

Hay and pasture is a very large portion of the feed that we feed cattle, and about 80 percent of the forage that the cattle use 9 months of the year or 10 months, depending upon your operation, there is a forage that is not available for any other use to the public, simply to feed cows.

WILDLIFE ON OUR RANCH

Now, on our ranch we have about 100 head of elk and about 400 head of whitetail deer and Canadian honkers and wild turkeys that most of them are the gift of the Montana Fish and Game Commission. But we do also feed these animals. And so our operation continually helps out people that like to hunt and fish.

REPAIRS, FUEL, AND MARKETING COSTS

Repairs and fuel, about 9 percent of this. And included in this 9 percent also are marketing costs. Now, when you sell a calf in an auction market, it's sold on a percentage basis. And it's really strange, you know, when the price of cattle come up, why, we suddenly start paying a commission on these calves are sold, but when the price goes down, why, then there is just a locked-in price that we pay on the cattle. So everyone has to make a living, but as the prices increase, also everyone else gets their act together and cashes in on it.

LABOR COSTS

Labor and management hired, about 5 percent. And like many cow-calf operations out West, they're family operations, and I don't even know if 5 percent is returned to the family for their labor. But if you have to hire cowboys and people, seasonal help during haying, this 5 percent pretty much makes up your labor costs.

And one thing that we are plagued with today, although right now is maybe a poor time, Senator Baucus, that we are testifying, because cattle are at an all-time high, finished cattle. We are looking at the top of the cycle, but this cattle cycle follows about a 10-year cycle and for those 6 or 7 years that we kind of suffer along and try to pay our bills, why, we play catchup for about 2 or 3 years. And that's where we are right now.

So this 1,100-pound steer today of course, when he's finished brings quite a bit more than the average.

INTEREST ON BORROWED MONEY

Interest on borrowed money of course is a very big segment of it, 17 percent of the total cost, because in order for us to cash-flow our operation, especially when we move the cattle into a feedlot, if I retain ownership of these cattle after we wean them, we background them, they go into a feedlot and if I want to pay the additional cost to have those cattle finished, why, we borrow money to do this. And also, any capital investments, if you have to buy a new pickup or tractor or something, this is a long-term investment; it usually takes about 5 years to pay it off.

And this interest is 17 percent, as it's shown there, and then another additional 8 percent would be the interest that, if you had this ranch to sell or if you had the money that you could invest in the stock market or CD's or something, this is about the going rate of what you would receive if you were not putting it back into your operation, which most of us do.

Taxes, insurance, overhead, 12.5 percent. And I think this does not need too much explanation. This varies, of course, pretty much per county and per State. And in Montana, we are one of the few States that still pay an average inventory tax on cattle. And very few other States do this. The reason that we have to do this is that for many counties in Montana that the only way that they maintain their schools and their roads is through the taxation of cattle. But it's the only inventory tax on any item in the State of Montana, but we still have to do this to support some of the counties that have no other tax base except cattle.

DEPRECIATION OF LIVESTOCK AND EQUIPMENT

Depreciation of livestock and equipment, this will run about 9.5 percent. Of course, we all realize that hopefully we can turn over our equipment in 5 or 6 years, but the way it has been with the drought and the poor market that we have had through the 1980's, it's not unusual for many operations to be driving a pickup that is 10 years old and using tractors that have anywhere from 5,000 to 8,000 hours. When we bought these tractors in the 1970's, you could buy the tractor for $12,500, and that same tractor today will cost you about $35,000. So you do have to figure the depreciation.

BREAK DOWN THE TOTAL COSTS ON THE PERCENTAGE

When we break down the total costs on the percentage, the grain and supplement, what we're looking at, 24 percent on a 1,100-pound steer is going to be about $182; hay and pasture, about $114; repairs, about $69; labor per calf will be about $38; taxes, insurance, $95; interest on borrowed money, which is about 25 percent of our total, will be $129; depreciation, about $72.

TOTAL COST

So on this steer, 1,100-pound steer, the total cost would be about $760 that we have in that steer by the time he goes to the packer. And today, of course, based on grade and yield and the quality of the steer, the price will vary anywhere from 78 cents to 80 cents a pound on a finished cattle.

THE BEST THAT STEER WILL BRING

Let's look at the best that steer will bring: 80 cents on an 1,100-pound steer, bring $880. And so the difference in the market there is $120 profit. And by the time you share this $120 profit between the cow-calf operator and the feeder, why, today we are making about $60 a head on these cattle.

This may seem like pretty good profit. But when you compare it probably to 2 or 3 years ago, when if you were making $6 or $8 a head on each animal it was very difficult for a small operator if you own your own cattle and background them and retain ownership through a feedlot, to make any kind of a profit on $6 or $8 a head. But like today, with the high price, we're looking at $60 profit. And so it's much easier to live with.

Some of the bigger feedyards that feed thousands of cattle, they buy these calves, and if they can make $20 or $30 a head on them, they realize a fairly equitable profit. And when we put these cattle into a feedlot and we have them custom-fed, why, all the costs and the labor and the yardage and everything is figured in, and regardless of what that finished cattle will bring, we still pay the same cost. And of course, that cost is based on their production cost and also they include 15 to 20 percent profit. And you will pay these costs regardless of what the market is and how well the calf does.

I think that about covers my presentation, Senator. If there are any questions at this time, I would certainly answer them.

Senator **Pryor**. Thank you very much, Jimmy.

Senator Baucus.

Senator **Baucus**. Thank you, Mr. Chairman.

Jimmy, taking the average price over, say, the cycle and then looking on down the road at your various components of the cost of production—you have outlined them here already this morning—which components of cost of production are most worrisome to you as compared to the average price you are going to get for your steers? As a family operation, what are you looking at down the road and what are your two sons looking at down the road? That is going to be more of a concern to them than perhaps some other factors?

Mr. **Wilson**. I think, Senator Baucus, in 1984-85, if you encouraged any of your children to come back to a farming ranch, it was a form of child abuse. [Laughter.]

Today, of course, it may look otherwise.

Senator **Baucus**. I have a brother that will agree with that.

Mr. **Wilson**. Well, that is true. We could not encourage our young people to come back. But on the other hand, I have two sons that worked off the ranch for 5 years after college. I insisted they get out and find something else to do. And the trade-off for them is to come back to Montana to be able to raise cattle. But you know, when they get married and have families, the way of life kind of goes out the window. They have to make a living, and especially if they marry a city girl, they have a very hard time making ends meet, and the girl considers a ranch a real macho operation, for men only. And it is a very tough, tough deal for the families to exist.

I think probably, in answering your question, interest costs are something that plague us constantly. You know, during hard times, the fuel dealer, the machinery dealer, the feed dealer in these small towns keep their prices down in order to be competitive. But once the price of cattle come up, the price of price of machinery and fuel and everything follows the price of the cattle up. But when the cattle come down, say, in 2 or 3 years, which is inevitable, they never seem to reduce their costs.

So we then go along with the prices that have been established during the high days that we have to live with maybe for another 5 or 6 years during the cycle. So I think that is one thing: the prices never follow us back down.

Senator BAUCUS. All right. Let me ask the question a little bit differently. Do you see your costs over the cycle rising more than steer prices, or do you see the costs projected to be about parallel with the average price over that period? I am just trying to get a sense of what are you looking at and what are your two sons looking at?

Mr. WILSON. Well, I think certainly the cost of energy is certainly not going to go down. And this is a large part of our operation. We pump water for irrigation. We pay electrical costs and also for fuel costs.

Senator BAUCUS. The cost of fuel has gone up.

Mr. WILSON. Yes. And I don't think that price is every coming down unless something is going to happen that we don't foresee. And it's inevitable. I mean we are going through unusual times at the present time. In Montana, 8 out of the last 10 years for Montana as a whole in the 1980's, were drought years, and about 800,000 cows moved out of Montana simply because we did not have the feed and the $100 hay. Even with the Government programs that helped us out, it was hard to maintain a cowherd.

Through supply and demand, what happens with the rancher is during good times when the prices start creeping up, people start building cattle numbers. And then as cattle numbers increase, of course, supply or demand—supply exceeds demand and so the prices start coming down. But you're still locked into your expenses. And so how you pay your expenses is by selling your basic cowherd. And by selling your basic cowherd, numbers start decreasing, and of course then demand will exceed supply, and the prices creep up.

With the drought that we have presently in the Nation, this has created, for instance, right now we are short of cattle in Montana. We have grass, but a man that has sold his cattle goes into a bank and he wants to borrow the money to buy back in, and the banker wants 30 or 40 percent down on these cattle. And it's very difficult. Even if he sold his cattle 4 years ago at a time when he got a fairly good price for them, it's very difficult to buy back in at these high prices.

Senator **Baucus**. All right. How do you handle the problem that faces a lot of cattle producers with respect to grain producers? The grain producers are also worried about their cost of production—if they're going to get a good net income. And cattle operators are worried about their cost of production. You're worried about your cost of production. How do you advise us to put those two components together here in a fair way for both the cattle producers as well as the grain producers?

Mr. **Wilson**. Well, if you look at the basic formula, in the past, finished cattle, with the exception of the last 2 or 3 years, the fat cattle price has been fairly consistent. Maybe $2 it would vary the whole year. So you're locked into the price that you're going to get for the end product.

All right. What makes up the formula is the price of feeder cattle plus the price of feed. I mean those are the two basic ingredients to reach a finished animal. If you're locked into the product and the grain prices go up and the feeder has to buy cattle and balance the formula, then he is going to have to turn around and buy feeder cattle cheaper.

It used to be that they said: high-priced grain, high-priced cattle. And that was the time when people were feeding cattle to the time that their feedbin was empty. But now where you're getting discount on cattle that are overfinished anywhere from $80 to $90 to $120 a head on overfat cattle, it makes feeders more conscious of their program.

And I am sorry, Senator, you may not like what I say, but I think if the Government stays out of the grain business and bases it on a market, free open market system, we are much better off than trying to supplement the grain industry to provide those people a living, because consequently what happens, it comes off on the cattle people. We must get away from helping one segment of the industry at the expense of the other.

Senator **Baucus**. Well, frankly, if our governments around the world are successful in the Uruguay round of the GATT in mutually reducing agricultural subsidies worldwide, we are going to get much more closer to that point.

Mr. **Wilson**. I agree.

Senator **Baucus**. That will be a major benefit to most American agricultural commodities. There are some little wrinkles with some commodities, but certainly cattle and wheat in our part of the country will be major beneficiaries if in fact the world mutually phases out agriculture price supports.

Mr. **Wilson**. Well, those of us in the cattle business, we have been accused of neglect of agriculture as a whole. But we have been trying to work this out, and I realize in the grain industry there is a problem, and if you're on top of a high building you can either jump off or walk down. And we simply do not want any disasters in the grain industry. But I feel that we must walk down in a manner that everybody can live with it and still those people have to make a living like the rest of us.

Senator **Baucus**. That's right. There is a balanced approach to that.

Mr. **Wilson**. That's right.

Senator BAUCUS. Jimmy, I appreciate your help very much. Thank you.

Mr. WILSON. Well, thank you, sir, for the invitation.

Senator PRYOR. Jimmy, thank you. And before you leave, I would like to say that we have a considerable amount of cattle production in the State of Arkansas, nothing like Senator Baucus' State of Montana. But we also have an enormous poultry industry, and I am constantly hearing from our own poultry industry there about too much involvement in grain prices and et cetera. So I am very sympathetic, I guess, to your particular problem, as a result of our own poultry industry.

You have given us some advice, I think. Both Senator Baucus and I sit there day after day trying to work out a balance in an agriculture bill between the citrus growers and having clean water and environmental concerns, herbicides, pesticides, and the commodities, the row crop issue, trying to treat all of the American farmers fairly and with some justice. And then sitting down at the other end of the room from us is the Secretary of Agriculture or his designee, saying if we do so-and-so or if we increase costs too much or taxes or exposure of the U.S. Department of Agriculture, that the President is going to veto the bill.

So we are sitting there trying to find, day after day, a balance that we can submit to the President, a balanced bill. Do you have any further advice to us as we proceed in drafting this 1990 farm bill?

Mr. WILSON. Well, hopefully that there will not be any major changes. It takes a period of time for everybody to settle in and work with the program, and I think you should be complimented in the last year, 5 years, that there were not any major changes. And naturally, times change and so programs have to change.

I would certainly like to thank you two Senators, Senator Baucus, for your work with helping us maintain our checkoff, which is probably the largest factor for a good cattle price.

Senator BAUCUS. I agree. That has worked out pretty well.

Mr. WILSON. And for your interest, Senator, in promoting beef in Japan, we certainly appreciate this.

Senator BAUCUS. Thank you very much.

Senator PRYOR. By the way, we are selling chickens in Japan now. So we are real proud of that.

Mr. WILSON. Well, you really don't want me to comment on that now. [Laughter.]

Senator PRYOR. Now, Jimmy, we have yet to sell them any rice there. I don't know when that day is going to come.

Mr. WILSON. Well, you know, traditionally those people have been rice eaters, and they get tired of it. And what do they do? They look to meat. And that is the name of the game. I mean it's a good, wholesome product, and we certainly want to pursue that. [Laughter.]

Senator PRYOR. Jimmy, let me, before you leave the witness table, acknowledge Senator Conrad Burns has just walked in. I motioned him up to the table today, but I believe he is going to participate in the audience.

Conrad, you are welcome to make a statement or to make a speech.

Senator **Burns**. I enjoy being an observer here.

Senator **Pryor**. Well, we appreciate your being here, Senator Burns. We certainly do.

We thank you very much, Mr. Wilson.

Mr. **Wilson**. Thank you.

Senator **Pryor**. We will continue with our next witness.

I think at this stage I am going to call—we have heard from a lot of farmers here this morning; we are going to hear from a few more before our lunch—I think I will call now the representative of the U.S. Department of Agriculture.

If you would just come to the table, Doctor, and just state your name, address, social security number so we will have that for the record. [Laughter.]

STATEMENT OF BRUCE L. GARDNER, ASSISTANT SECRETARY FOR ECONOMICS, U.S. DEPARTMENT OF AGRICULTURE, WASHINGTON, DC

Mr. **Gardner**. Thank you, Mr. Chairman, Senator Baucus. I am Bruce Gardner, the Assistant Secretary for Economics. I appreciate the opportunity to appear.

Senator **Pryor**. Thank you, Bruce.

Mr. **Gardner**. I will give a little of the Department's views.

Senator **Pryor**. Could you please speak up, sir? We are having trouble hearing you.

Mr. **Gardner**. I appreciate the opportunity to appear to discuss farmers' costs of production. A lot of the points that have been made have used Department of Agriculture data, and I was very pleased to hear that they were just used and not criticized. We have had some problems in the past, sometimes, with people wanting to revise the data, and so on. I think we have tried to improve them over the years, and I am glad to see people using them as they are.

Senator **Pryor**. Well, we are using it, but that does not keep us from ultimately criticizing it. [Laughter.]

Mr. **Gardner**. Oh, I see.

Senator **Pryor**. Bruce, I have really have some problems here because none of the farmers in our State have indicated to me that during that 1985 year, give or take, that there was such a decline in the costs of producing food and fiber in this country. But maybe you can back that up a little bit. So you're on your own, if you would like to.

COULD YOU EXPLAIN THE DECLINE IN THE COSTS OF PRODUCING FOOD AND FIBER?

Mr. **Gardner**. Well, between 1984 and 1986 there was a fairly sharp decline in energy prices. The fuel and energy component of prices paid fell fairly substantially in that 2-year period, and in fact is still at about the level it was in 1981.

But during the mideighties there, there was a substantial decline in fuel and energy prices, which are volatile, of course, and have come back up some since. Also, the fertilizer price fell approximately 20 percent, I believe, between 1984 and 1987, on an U.S. average basis. So that is coming into some of these cost of production estimates.

Senator Pryor. All right. Now, once again using your figures—I am going to allow you to make your statement momentarily—we have talked about the decline in cost of production that your figures indicate. Also, I don't think that you would argue with your own figures that we are seeing a rapid acceleration now at this stage, an upward spiral in the cost of production at this moment. Is this correct?

Mr. Gardner. Well, it is certainly not declining as it was before. I don't think it has been an extremely sharp increase in these prices of inputs, but they are increasing whereas they were falling.

Senator Pryor. Well, we will discuss that later.

Mr. Gardner. I might mention too that it depends on the concept you use. On your charts that we have here, the one that really comes down a lot on the cost of production estimates is corn, over here. And that, I believe, is a different cost measure, that is, cash expenses plus some imputed costs, whereas most of the others are what we call total economic costs. And this particular one (corn) is very heavily influenced by interest expenses and interest rates. Actually if you had the total corn cost on the same basis as these other ones, it would look very similar and it wouldn't show you quite that sharp a decline.

With that, if I may, Mr. Chairman, I would like to make a couple of remarks about some written testimony that I have submitted.

Senator Pryor. Certainly. Your prepared statement will be included in the record.

USDA METHODS AND PROCEDURES

Mr. Gardner. My prepared testimony has some data on some of these facts we have been discussing. I would like just to emphasize a couple of them here.

THE COST OF PRODUCTION IS A SEEMINGLY SIMPLE CONCEPT, IT IS QUITE SLIPPERY AND COMPLICATED TO MEASURE IT PRECISELY

One is that although the cost of production is a seemingly simple concept, it is quite slippery and complicated to measure it precisely. And it is particularly tricky to attempt to provide a kind of scientifically justified or fair adjustment in support prices by linking support prices to cost of production.

COST OF PRODUCTION

Now, why is this so? The basic elements of cost of production are straightforward. We have the value of seed, fertilizer, fuel, other inputs that are necessary to produce a unit of output. But production involves many inputs whose costs are far from straightforward to estimate. For example, the operator's labor, what wage rate should we use to value that labor? How much labor, including the managerial activity that is necessary, is actually used by a farmer on a particular crop?

Capital equipment owned by the farmer poses even more difficult problems. A machine is not used up in producing a crop, but it depreciates. Estimating the exact amount of this depreciation is a difficult matter.

And finally, land costs are equally tricky to estimate, unless in some cases, as we do, we have a cash rental rate that gives you a notion of that cost.

USDA ROLE

Despite these difficulties, USDA has been providing measures of costs of production for many years. These estimates have been mandated by Congress since 1973. The statistical base for these estimates has been improved considerably over time, and the underlying data now come from a survey of some 25,000 farmers each year. At times these estimates have been used in establishing target prices and other support prices. There are proposals to use cost measures to readjust or index support prices in the 1990 farm bill.

The Agriculture and Food Act of 1981 established a National Agricultural Cost of Production Standards Review Board. This Board is composed of 11 members—7 commercial farmers, 3 nonfarmers, and 1 USDA employee. The Board reviews all aspects of USDA cost of production estimates and makes recommendations to the Secretary of Agriculture for changes.

In 1983, the Board recommended that USDA estimate cost of production excluding the effects of Government programs. The reason for excluding the effects of Government programs is the belief that if we include the effects, then costs are going to be overstated as a means of determining whether support prices are at an adequate level.

EXAMPLE OF THE PROBLEM

The clearest example of the problem arises for a farm which is cropped by a tenant under a crop-sharing agreement. Imagine that situation. In this case, the cost of land to the tenant is clearly and explicitly a function of the price of the commodity, including any deficiency payments. If the target price is increased, then the rental cost of land automatically rises. In order to adjust for this effect, USDA now excludes deficiency payments from the price of commodities used in estimating crop-sharing land rentals.

This exclusion has led some to argue that the land rental rate used in USDA's calculation understates the real-world rent that farmers must pay in order to produce the crop that has a deficiency payment. And this is true, but the real-world rent includes payment for the right to receive these deficiency payments. So if you raise the target price, this will automatically raise land rents, and if you include these rents in costs and use cost to set target prices, then you have the result that every increase in target prices is going to generate the need for a further increase.

The same sort of problem exists in the longer term. That is, there is no way that raising the target price can permanently move price above costs that include land values in that cost estimate. And this is because the value of the deficiency payment is in fact a return to the ownership of the acreage base, and that is tied to the farmer's land. So in fact, even USDA's cost of production estimates that attempt to exclude the effects of government programs still include these effects to some extent.

Overall then, attempts to balance target prices across commodities by comparing costs or adjusting all target prices by a cost index over time I believe is more likely to create problems than to solve them.

The best approach might be, although I don't know that any indexing is appropriate, but you would like to set your target prices to fit supply and demand conditions so that you don't get the target price far out of line with the prices that supply and demand conditions justify; for example, as we attempt to do in dairy support prices.

With that, let me stop and attempt to answer any questions you might have.

[The prepared statement and attachments of Mr. Gardner follow:]

STATEMENT OF
BRUCE GARDNER
ASSISTANT SECRETARY FOR ECONOMICS
U.S. DEPARTMENT OF AGRICULTURE
BEFORE THE
SENATE COMMITTEE ON AGRICULTURE, NUTRITION, AND FORESTRY
SUBCOMMITTEE ON AGRICULTURAL PRODUCTION AND
STABILIZATION OF PRICES

April 23, 1990

Mr. Chairman and Members of the Subcommittee, I appreciate the opportunity to discuss farmers' costs of production. My remarks cover USDA's role in providing estimates of costs of production, the methods used to compute the estimates, and problems in linking support prices to changes in costs of production.

USDA Role

The Agriculture and Consumer Protection Act of 1973 mandated the Secretary of Agriculture to conduct a study of costs of production for wheat, feed grains, cotton, and dairy commodities and establish a national average cost of production. These estimates are prepared by the Department's Economic Research Service (ERS) and published annually. The 1973 Act did not specify any uses for the estimates. However, the Food and Agricultural Act of 1977 required that cost of production estimates--including variable, machinery ownership, and overhead costs--be used to adjust target prices for corn, wheat, cotton, and rice for the 1978-81 crop years.

The Agriculture and Food Act of 1981 revised the 1973 statutory wording to "... include all typical variable costs, including interest costs, a return on fixed costs, and a return for management." However, the 1981 Act abandoned the production cost formula for adjusting target prices and instead set escalating minimum target prices based upon expected inflation rates.

The 1981 Act also established a National Agricultural Cost of Production Standards Review Board. This Board is composed of eleven members--seven commercial farmers, three nonfarmers knowledgeable about costs of production, and one USDA member. The purpose of the Board is to review the adequacy, accuracy, and timeliness of methods used by USDA to make cost of production estimates and to then make appropriate recommendations to the Secretary. The Board was renewed in the Food Security Act of 1985. The 1985 Act also required cost of production estimates for peanuts and sugar, but contained no specific language addressing components of cost of production estimates or procedures. Thus, the 1973 legislative language regarding costs of production estimates, as amended in 1981, remains in effect.

USDA Methods and Procedures

The concept of production cost, for example, the cost of producing a bushel of wheat, is simple and straightforward at first glance. It is just the outlays that a producer must make in order to grow a bushel of wheat. But when actually trying to measure the cost of production, the idea becomes slippery and complex. We need to measure:

- The quantities of each input used.
- The price of each input.

- The amount of output that the inputs generate.

In the same way that a producer knows some production cost items better than others, the USDA estimates are built up from data having varying levels of uncertainty. Cash expenses are short-term out-of-pocket expenses that are the easiest to estimate. They may be determined with reasonable accuracy from the farm's record books, sales receipts, and so on. Other cost components are more complex and difficult to estimate. Capital replacement measures the machinery and equipment used up in production, not purchased capital. Equipment used in the farm's entire operation must be allocated to each commodity. Fuel use, machine life, and purchase price must all be estimated.

Other elements of costs involve added difficulties and sources of error. Total economic costs include cash expenses, capital replacement, and returns to operating capital, other nonland capital, land, and unpaid labor. These returns are computed in various ways. For example, the returns to capital are imputations based on the opportunity cost of capital, the historical rate of return on capital, and the value of the nonland capital. On the other hand, unpaid labor is determined by first computing the commodity's total labor requirement valued at average wage rates for hired farm workers. Then, any expenses for hired farm workers are subtracted. What is left is a return to family or other unpaid labor. The point is that production cost data involve many constructed ingredients. The further we depart from variable cash expenses, the more problematic the data. Moreover, the cost per unit of output is greatly affected by the variations in yield so that, for example, in a drought year the cost of producing the wheat actually harvested is very high.

Data that go into USDA cost of production estimates are gathered in an annual probability survey which contacts about 25,000 farms. This probability survey allows for regional and national estimates that are statistically reliable on such information as field operations, size and type of equipment, fertilization rates, seeding rates, custom operations, rental rates, and labor use as well as price and quantity data for production inputs.

Because of survey costs, the Department cannot survey each major commodity every year; therefore, each crop or livestock enterprise is surveyed on a four-year rotation. Between surveys, costs of production estimates are updated using recent yields and input prices and price indexes. Quantity rates per acre of most inputs are held constant for purposes of calculating costs each year between survey periods.

The most comprehensive cost of production estimate is for "total economic costs". Economic costs consist of cash expenses less interest charges, capital replacement costs, and imputed returns for operating capital, machinery, land, and unpaid labor (not hired). Total economic costs allow for comparisons among farmers that have different equity levels or tenure arrangements.

Details of the components of total economic costs and other cost concepts are given in Table 1.

Recent Cost of Production Changes

Over the past 5 years, the index of prices paid by farmers has increased 11 percent, well below the 17-percent gain during the first half of the 1980's and the 55-percent rise during the last half of the 1970's. The large increases during the late 1970's stemmed from more than two-fold increases in fuels, energy, and interest expenses. Also, farm equipment and wage rates increased by about half during this time of double-digit inflation. During the first half of the 1980's, the rate of increase in prices paid by farmers slowed quickly as inflation fell to 3-4 percent annually by the mid-1980's. Still, prices paid for seed, agricultural chemicals, farm equipment, and interest expenses increased by about 30 percent during the first half of the 1980's, compared with the overall prices paid increase of 17 percent. By the early 1980's, interest charges had become farmers' single largest production expense, totaling over $20 billion annually.

Continued modest inflation during the second half of the 1980's helped to further ease the rise in input prices. Interest rate charges for 1990 are expected to be 22 percent below 1985 and interest expenditures for all of agriculture are expected to be some $7 billion below the 1982 peak. Prices of fuels and energy have also shown a decline of 5 percent since 1985, despite more recent rises. Otherwise, only prices paid for farm equipment, including automobiles and trucks, and wage rates have increased substantially more than the 11 percent rise in overall prices paid by farmers since 1985.

Between 1980 and 1985, cost of production increases for the major program commodities including soybeans averaged about 11 percent compared with a 40 percent rise during the last half of the 1970's. Over this period cotton costs of production rose 28 percent, rice 11 percent, corn 10 percent, soybeans 6 percent, and wheat 2 percent. During the 1980-85 period, data on input quantities used show farm labor and machinery inputs declined more than land inputs, indicating less labor and machinery use per acre at the end of the period. Agricultural chemical inputs remained unchanged while land inputs declined, indicating greater per acre chemical use by 1985.

Between 1985 and 1988, the last year for which official estimates are available by commodity, costs of production for the four major program crops plus soybeans declined an average of 4 percent. Over these 3 years, corn costs of production declined 17 percent, both rice and wheat declined 4 percent, but cotton costs increased 1 percent, and soybeans 6 percent. Considerably lower interest rates and lower fuel and energy costs helped to hold down overall costs over these 3 years. Although official estimates are not available by commodity for 1989 and 1990, costs for the major crops will likely be up moderately in these 2 years since the index of prices paid for production items for 1990 is expected to be up about 6 percent from 1988.

Problems in Using Production Cost Data in Policy Determination

Problems arise when we try to compare costs with commodity prices. People often refer to price levels sufficient to cover costs as if the cost of producing a bushel of wheat were a fact that exists independently of the market price of wheat. But, this independence does not exist. If the price of wheat rises substantially, that fact in itself will increase the amount that farmers are willing to pay for rented land, and it will increase the amount that landlords will charge for that land. Moreover, if high prices encourage an expansion of acreage, the prices of seed and other specialized inputs are also likely to rise. Therefore, when price rises, cost of production will rise also. Indeed, a condition for equilibrium in a competitive market is that the price equals the average cost of production. If price is greater than the average cost, we expect production to expand until either costs are bid up or the price of the product is bid down by the extra output. In this sense, a cost-price squeeze is inevitable in agriculture as in other competitive industries. This is true even in extreme cases such as Saudi Arabia where the government offered prices approaching $20 per bushel for wheat. In response to these prices, producers grew wheat up to the point that the cost of irrigation as well as the other inputs used amounted to roughly the price offered.

Another problem with attempting to set target prices or price supports to cover cost of production is that this approach can lead to a cost-price spiral that is self-perpetuating. Higher target prices result in higher land costs, which increases overall production costs. A recent ERS study concluded that 90 percent of the increase in rice production costs coming from government support were in the form of increased land costs. Thus, government payments through the target price mechanism boost land prices and production costs; these higher costs lead to even higher target prices when such supports are linked to costs of production increases.

Under the 1973 Act, target prices (except for rice) for 1974 and 1975 were set in relation to estimated costs of production and then adjusted upward in 1976 and 1977 based on increases in the prices paid index. The 1977 Act further adjusted all target prices upward based upon estimated cost of production increases. Although not explicitly tied to costs of production, target prices under the 1981 Act were increased about 6 percent annually based upon anticipated inflation that never materialized. As an example, the corn target price went from $1.38 per bushel in 1975 to $3.03 in 1984, an increase of 120 percent in 10 years. With target price protection applying to rising program yields and plantings (over most of that period), by 1982 grain supplies were record high, exports were declining as domestic prices exceeded world prices, and program costs were soaring. These conditions led to the combined ARP and payment-in-kind program in 1983, the largest annual acreage reduction program in history.

Milk supports also provide a classic example of what happens when price supports are escalated. From 1973 to 1980, the milk price support was adjusted at 9-month or 6-month intervals to reflect 80 percent of parity. Under these adjustments, the milk price support increased from $5.29 per hundredweight in March 1973 to $13.10 in October 1980, an increase of 148 percent in 7.5 years. A further increase in the support price to $13.49 was made in 1981. CCC removals went from 2 billion pounds, milk equivalent, in 1973 to nearly 17 billion pounds by 1983, and the cost of the dairy program rose from $200-300 million annually to over $2.0 billion. Meanwhile, milk production rose from 115 billion pounds to 140 billion.

The dairy example illustrates another problem in comparing costs to prices that results from the existence of by-products or joint products. For every 15,000 pounds of milk, a producer can expect to get one calf, and for every 50,000 pounds there will be one cull cow. If the cow and calf sell for $700, the returns work out to roughly $1.50 per hundredweight of milk. Therefore, if the cost of production of milk is $10.50, the break-even price of milk is $9.00, not $10.50.

Other examples of the joint-product type are that a legume reduces the costs of producing a succeeding row crop by fixing nitrogen, that winter wheat may be grazed as well as harvested, or that a crop of wheat and soybeans can be grown successively on the same field in the same year. In each case complications arise that are difficult to capture accurately in comparing costs and prices.

The Cost of Production Standards Review Board recommended that USDA estimate a cost of production measure that would be independent of government payments. This has proven impossible to carry out in a simple, yet accurate way. For example, an obvious way in which government payments affect the cost of production is with respect to the land cost for a share-cropping tenant. The landlord's share in value terms depends on the value of the crop, including government payments. In order to remove the effect of government payments, ERS calculates the share rental rate by subtracting the per-acre expenses covered by the landlord from the per-acre value of production that goes to the landlord (excluding government payments). But, consider the situation for a producer similar in every respect, but who rents on a cash basis. In this case, the landlord will still receive the same rental rate, but ERS cannot exclude the effects of government payments because the rental payment is contracted for independently of commodity price even though, in fact, the amount of rent paid in the market situation will depend on the expectation of price including government payments. So even the cost of production estimate excluding government payments still is increased by the existence of payments.

Another problem with using cost of production to adjust income and price supports is that cost of production data represent an average per planted acre for the commodity sector as a whole and do not provide information on differences in cost by region and by size of farm. For example, our most recent distributional data for corn for 1987 show that farms with less than 25 acres of corn in 1987 had average cash expenses of about $1.83 per bushel, while producers with 100 to 500 acres of corn had average cash expenses of $1.34 per bushel. Cash expenses per acre were about the same for the two farm classes, but yields for the larger farms averaged 121 bushels per acre compared with 91 bushels for the smaller farms. Thus, cost of production estimates do not necessarily reflect the costs of production of commercial farms who largely depend upon farming for their livelihood.

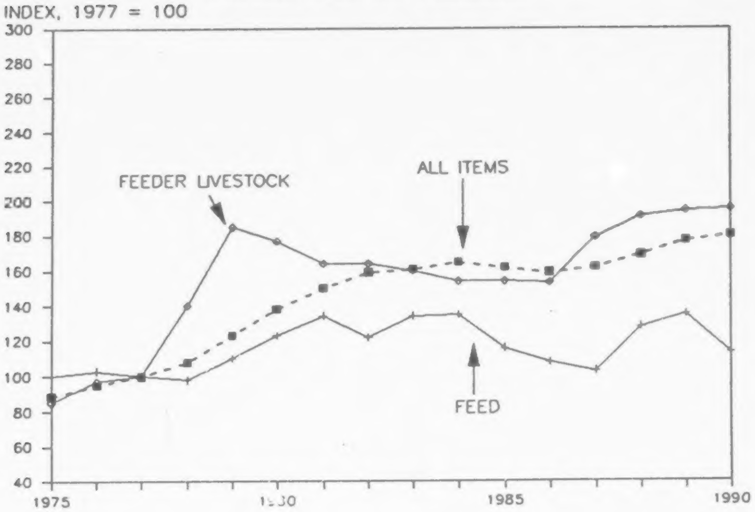
In sum, cost of production, or a prices paid index, do not provide a scientific or "fair" basis for adjusting support prices. There is no "right" cost of production. Attempts to index support prices in the past have led to costly policies which proved unsustainable and in the end created more problems than they solved, such as the farm sector experienced in the first half of the 1980's. I hope that we do not gamble on going down that road again.

I would be happy to respond to any questions.

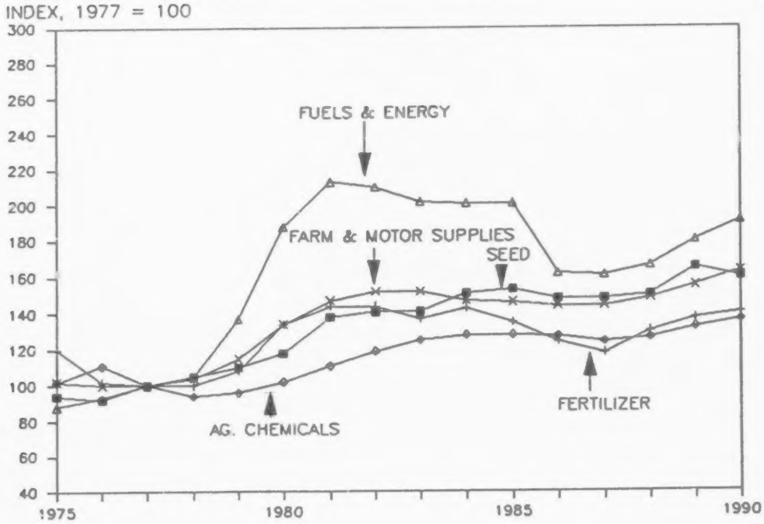
TABLE 1: COST OF PRODUCTION ESTIMATES

Cost Category	Items Included	Examples
Variable Cash Expenses	Seed, fertilizer, lime, chemicals, custom operations, fuel, energy, repairs, hired labor, irrigation water, drying, and technical services	Farm records on purchases of herbicides
Fixed Cash Expenses	Taxes, insurance, interest on operating and real estate loans	Farm records on interest payments
Total Cash Expenses	Variable cash expenses plus fixed cash expenses	
Capital Replacement	Machinery and equipment used up to produce the commodity	Machine hours of a a combine times total hourly operating cost
Total Economic Costs	Variable cash expenses, farm overhead, taxes, insurance, capital replacement plus:	
	Return to operating capital	Imputed: opportunity cost of capital (6-mo. Treasury Bill rate) times variable expenses
	Return to other nonland capital	Imputed: value of machinery times estimated real rate of return to all production assets for farm sector
	Return to land	Imputed: average of cash and share rental values less real estate taxes
	Unpaid labor	Total labor requirements valued at average farm wage rates less hired labor costs

PRICES PAID BY FARMERS



PRICES PAID BY FARMERS



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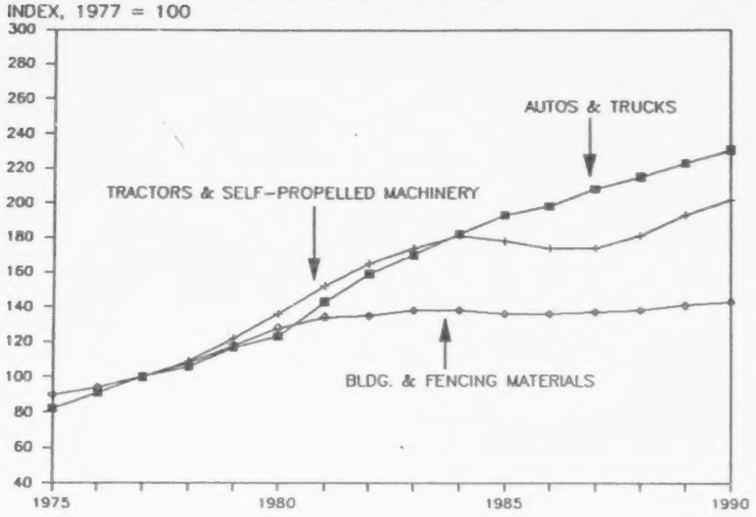
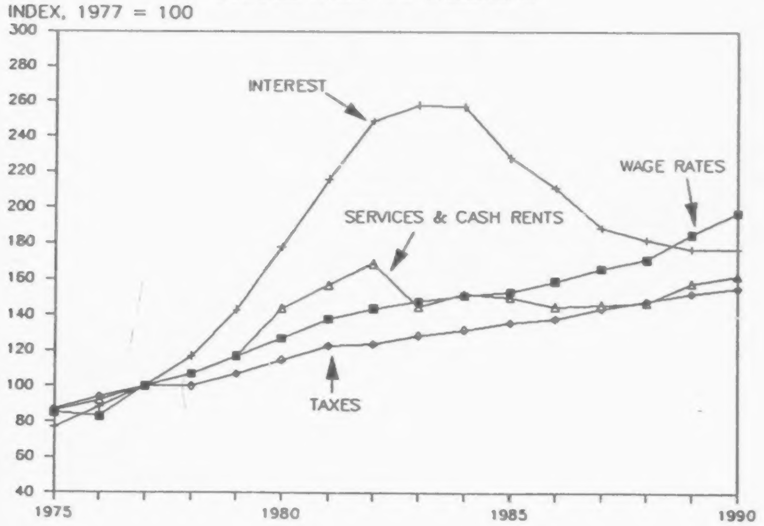
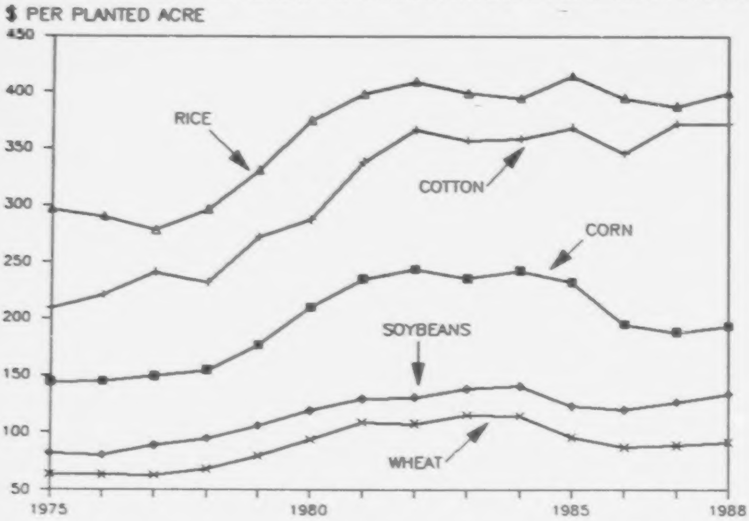


PRICES PAID BY FARMERS

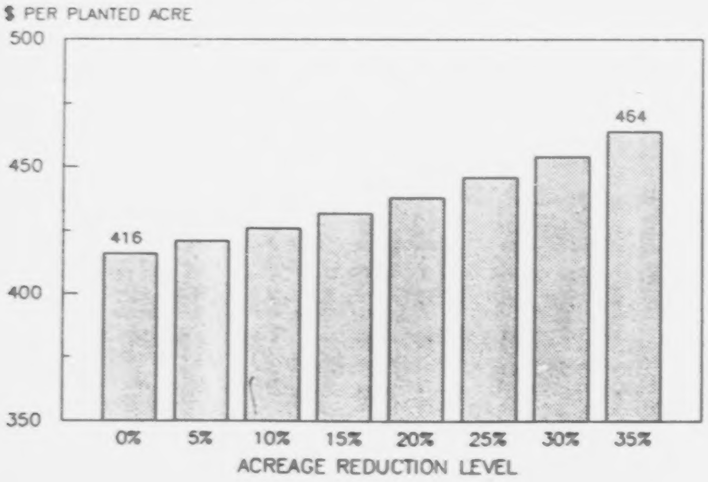


USDA ESTIMATES OF COST OF PRODUCTION FOR MAJOR CROPS 1/



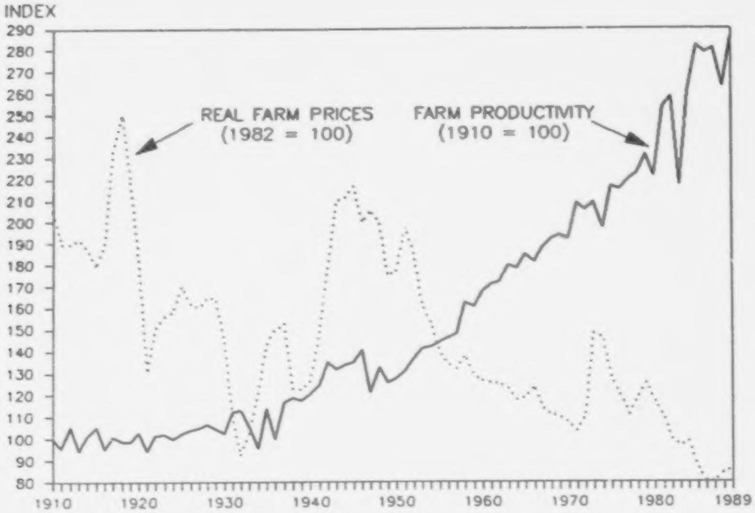
1/ Total cash costs plus capital replacement cost.

RICE COST OF PRODUCTION AT VARIOUS ACREAGE REDUCTION LEVELS 1/

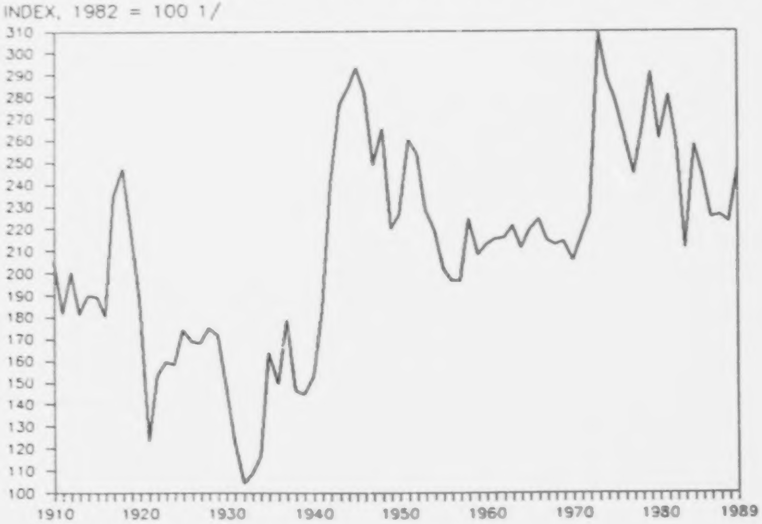


1/ Total cash costs plus capital replacement cost (fixed cost spread over fewer acres as acreage reduction percent increaes). Estimate for 1990.

REAL FARM PRICES AND FARM PRODUCTIVITY

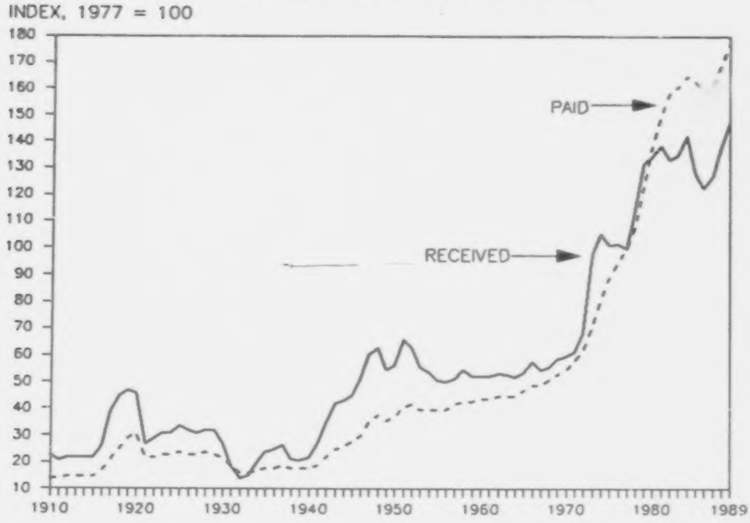


INDEX OF REAL FARM PRICES ADJUSTED FOR PRODUCTIVITY GROWTH

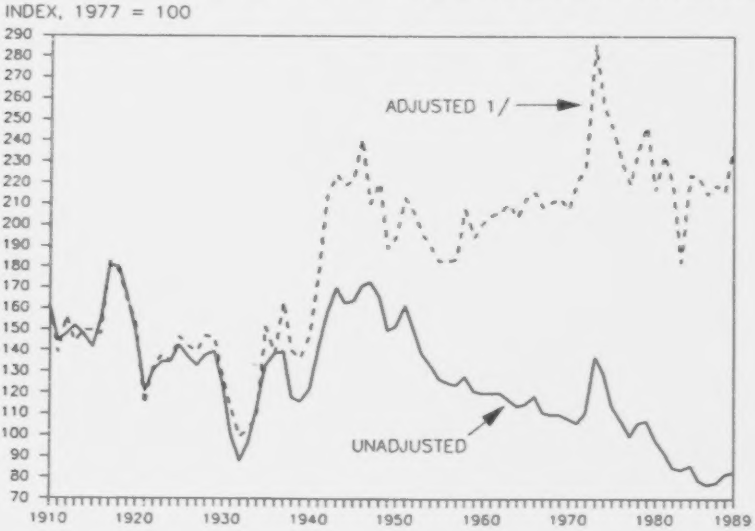


1/ Index of real farm prices, 1982 = 100, adjusted by farm productivity index where 1910 = 100.

FARM PRICES RECEIVED AND PAID



FARM PRICES RECEIVED-TO-PAID RATIO ADJUSTED FOR PRODUCTIVITY



1/ ADJUSTED FOR PRODUCTIVITY INCREASES SINCE 1910.

U.S. corn production costs and returns per planted acre, 1986-88 1/, 2/

Item	1986	1987	1988
		Dollars	
Gross value of production:			
Primary crop	167.60	186.02	216.39
Total	167.60	186.02	216.39
Cash expenses:			
Seed	19.25	18.86	18.87
Fertilizer	38.51	35.25	43.07
Lime and gypsum	2.26	2.25	2.30
Chemicals	20.27	20.19	20.16
Custom operations	5.37	5.39	4.76
Fuel, lubrication, and electricity	9.01	10.60	10.57
Repairs	8.10	8.25	8.14
Hired labor	7.87	7.83	7.87
Purchased irrigation water	.31	.31	.32
Drying	9.21	8.20	5.90
Technical services	.25	.26	.26
Total, variable cash expenses	120.41	117.39	122.22
General farm overhead	10.42	10.15	10.81
Taxes and insurance	13.81	14.65	14.61
Interest on operating loans	7.71	5.45	4.91
Interest on real estate	13.25	10.66	10.03
Total, fixed cash expenses	45.19	40.91	40.36
Total, cash expenses	165.60	158.30	162.58
Net returns less cash expenses 3/	2.00	27.72	53.81
Capital replacement	29.77	30.08	31.01
Net returns less cash expenses and capital replacement	-27.77	-2.36	22.80
Economic (full ownership) costs:			
Variable cash expenses	120.41	117.39	122.22
General farm overhead	10.42	10.15	10.81
Taxes and insurance	13.81	14.65	14.61
Capital replacement	29.77	30.08	31.01
Allocated returns to owned inputs:			
Return to operating capital 4/	2.53	2.75	3.41
Return to other nonland capital 5/	5.29	5.95	6.79
Net land return 6/	41.19	43.86	52.47
Unpaid labor	19.70	20.04	21.26
Total, economic costs	243.12	244.87	262.58
Residual returns to management and risk 7/	-75.52	-58.85	-46.19
Harvest-month price (dollars per bushel)	1.41	1.57	2.60
Yield (bushels per planted acre)	118.46	118.83	83.15

1/ Excludes direct effects of Government programs on costs and returns. 2/ Sum of operator and landlord costs and returns 3/ Gross value of production less total cash expenses. 4/ Variable expenses multiplied by time between use and harvest and by 6-month U.S. Treasury bill rate. 5/ Value of machinery and equipment multiplied by longrun real rate of return to production assets in the farm sector. 6/ Rental value based on composite share and cash rent. 7/ Gross value of production less total economic costs.

U.S. cotton production costs and returns per planted acre, 1986-88 1/, 2/

Item	1986	1987	1988
		Dollars	
Gross value of production:			
Primary crop	225.95	442.64	323.32
Secondary crop	29.73	46.61	57.99
Total	255.68	489.25	381.31
Cash expenses:			
Seed	6.23	8.16	8.03
Fertilizer	23.16	22.21	25.98
Lime and gypsum	.44	.41	.40
Chemicals	44.23	44.44	45.69
Custom operations	10.32	11.87	11.89
Fuel, lubrication, and electricity	22.60	26.91	27.92
Repairs	19.74	20.27	21.44
Hired labor	37.69	40.16	40.99
Purchased irrigation water	8.47	9.49	9.55
Ginning	43.37	65.26	55.93
Technical services	1.59	1.56	1.54
Total, variable cash expenses	217.84	250.74	249.36
General farm overhead	21.29	21.59	22.97
Taxes and insurance	12.66	13.76	13.99
Interest on operating loans	21.84	15.54	13.81
Interest on real estate	22.17	18.68	17.27
Total, fixed cash expenses	77.96	69.57	68.04
Total, cash expenses	295.80	320.31	317.40
Net returns less cash expenses 3/	-40.12	168.94	63.91
Capital replacement	50.35	51.65	54.59
Net returns less cash expenses and capital replacement	-90.47	117.29	9.32
Economic (full ownership) costs:			
Variable cash expenses	217.84	250.74	249.36
General farm overhead	21.29	21.59	22.97
Taxes and insurance	12.66	13.76	13.99
Capital replacement	50.35	51.65	54.59
Allocated returns to owned inputs:			
Return to operating capital 4/	5.09	5.98	6.94
Return to other nonland capital 5/	8.76	9.99	12.03
Net land return 6/	51.44	83.48	72.51
Unpaid labor	20.65	21.36	21.67
Total, economic costs	388.08	458.55	454.06
Residual returns to management and risk 7/	-132.40	30.70	-72.75
Harvest-month price (dollars per pound)	0.49	0.65	0.54
Yield (pounds per planted acre)	462.97	683.29	594.94

1/ Excludes direct effects of Government programs on costs and returns. 2/ Sum of operator and landlord costs and returns. 3/ Gross value of production less total cash expenses. 4/ Variable expenses multiplied by time between use and harvest and by 6-month U.S. Treasury bill rate. 5/ Value of machinery and equipment multiplied by longrun real rate of return to production assets in the farm sector. 6/ Rental value based on composite share and cash rent. 7/ Gross value of production less total economic costs.

U.S. rice production costs and returns per planted acre, 1986-88 1/, 2/

Item	1986	1987	1988
		Dollars	
Gross value of production:			
Primary crop	218.41	263.89	370.33
Total	218.41	263.89	370.33
Cash expenses:			
Seed	19.89	21.01	22.16
Fertilizer	35.34	30.96	36.28
Chemicals	42.06	39.06	40.30
Custom operations	36.52	35.49	36.58
Fuel, lubrication, and electricity	37.53	47.10	46.93
Repairs	22.24	23.34	24.49
Hired labor	39.34	39.09	39.36
Purchased irrigation water	9.12	8.30	8.28
Drying	43.32	39.08	39.92
Miscellaneous	1.29	1.29	1.31
Technical services	.56	.47	.48
Total, variable cash expenses	287.21	285.19	296.09
General farm overhead	20.77	20.28	21.50
Taxes and insurance	11.24	12.02	12.13
Interest on operating loans	22.56	15.89	14.04
Interest on real estate	12.54	10.16	9.42
Total, fixed cash expenses	67.11	58.35	57.09
Total, cash expenses	354.32	343.54	353.18
Net returns less cash expenses 3/	-135.91	-79.65	17.15
Capital replacement	40.69	44.27	46.34
Net returns less cash expenses and capital replacement	-176.60	-123.92	-29.19
Economic (full ownership) costs:			
Variable cash expenses	287.21	285.19	296.09
General farm overhead	20.77	20.28	21.50
Taxes and insurance	11.24	12.02	12.13
Capital replacement	40.69	44.27	46.34
Allocated returns to owned inputs:			
Return to operating capital 4/	5.01	5.64	6.68
Return to other nonland capital 5/	7.65	9.08	10.86
Net land return 6/	25.59	34.04	57.84
Unpaid labor	23.20	23.54	23.70
Total, economic costs	421.36	434.06	475.14
Residual returns to management and risk 7/	-202.95	-170.17	-104.81
Harvest-month price (dollars per hundredweight)	3.83	4.83	6.78
Yield (hundredweight per planted acre)	56.97	54.67	54.61

1/ Excludes direct effects of Government programs on costs and returns. 2/ Sum of operator and landlord costs and returns. 3/ Gross value of production less total cash expenses. 4/ Variable expenses multiplied by time between use and harvest and by 6-month U.S. Treasury bill rate. 5/ Value of machinery and equipment multiplied by longrun real rate of return to production assets in the farm sector. 6/ Rental value based on composite share and cash rent. 7/ Gross value of production less total economic costs.

U.S. soybean production costs and returns per planted acre, 1986-88 1/

Item	1986	1987	1988
		Dollars	
Gross value of production:			
Primary crop	150.64	171.66	200.25
Total	150.64	171.66	200.25
Cash expenses:			
Seed	10.82	11.16	11.91
Fertilizer	5.01	5.00	6.32
Lime and gypsum	.34	.29	.30
Chemicals	12.37	12.34	12.34
Custom operations	4.01	3.98	4.04
Fuel, lubrication, and electricity	7.39	8.97	9.12
Repairs	6.56	6.63	7.29
Hired labor	2.53	2.62	2.80
Technical services	.05	.05	.05
Total, variable cash expenses	49.08	51.04	54.17
General farm overhead	7.87	10.81	12.37
Taxes and insurance	13.46	13.94	14.35
Interest on operating loans	6.79	6.48	5.90
Interest on real estate	11.37	12.54	13.22
Total, fixed cash expenses	39.49	43.77	45.84
Total, cash expenses	88.57	94.81	100.01
Net returns less cash expenses 2/	62.07	76.85	100.24
Capital replacement	31.48	31.84	34.01
Net returns less cash expenses and capital replacement	30.59	45.01	66.23
Economic (full ownership) costs:			
Variable cash expenses	49.08	51.04	54.17
General farm overhead	7.87	10.81	12.37
Taxes and insurance	13.46	13.94	14.35
Capital replacement	31.48	31.84	34.01
Allocated returns to owned inputs:			
Return to operating capital 3/	1.08	1.24	1.51
Return to other nonland capital 4/	5.07	5.72	7.01
Net land return 5/	43.63	45.56	51.89
Unpaid labor	9.53	9.86	10.55
Total, economic costs	161.21	170.01	185.86
Residual returns to management and risk 6/	-10.57	1.65	14.39
Harvest-month price (dollars per bushel)	4.57	5.07	7.53
Yield (bushels per planted acre)	32.94	33.83	26.60

1/ Sum of operator and landlord costs and returns. 2/ Gross value of production less total cash expenses. 3/ Variable expenses multiplied by time between use and harvest and by 6-month U.S. Treasury bill rate. 4/ Value of machinery and equipment multiplied by longrun real rate of return to production assets in the farm sector. 5/ Rental value based on composite share and cash rent. 6/ Gross value of production less total economic costs.

U.S. wheat production costs and returns per planted acre, 1986-88 1/. 2/

Item	1986	1987	1988
		Dollars	
Gross value of production:			
Primary crop	66.06	76.21	95.71
Secondary crop	2.06	2.18	3.66
Total	68.12	78.39	99.37
Cash expenses:			
Seed	7.29	6.62	6.83
Fertilizer	12.93	11.75	14.08
Lime and gypsum	1.60	1.32	1.25
Chemicals	4.06	3.91	3.84
Custom operations	3.94	3.92	3.81
Fuel, lubrication, and electricity	6.74	7.56	7.48
Repairs	6.17	6.32	6.40
Hired labor	2.54	2.53	2.58
Purchased irrigation water	.22	.20	.20
Technical services	.18	.17	.16
Total, variable cash expenses	45.67	44.30	46.63
General farm overhead	4.69	6.01	6.87
Taxes and insurance	7.92	8.11	8.12
Interest on operating loans	3.83	3.36	3.49
Interest on real estate	5.25	6.73	6.06
Total, fixed cash expenses	21.69	24.21	24.54
Total, cash expenses	67.36	68.51	71.17
Net returns less cash expenses 3/	.76	9.88	28.20
Capital replacement	19.90	20.33	20.57
Net returns less cash expenses and capital replacement	-19.14	-10.45	7.63
Economic (full ownership) costs:			
Variable cash expenses	45.67	44.30	46.63
General farm overhead	4.69	6.01	6.87
Taxes and insurance	7.92	8.11	8.12
Capital replacement	19.90	20.33	20.57
Allocated returns to owned inputs:			
Return to operating capital 4/	1.38	1.46	1.79
Return to other nonland capital 5/	3.66	4.18	4.76
Net land return 6/	23.30	24.98	31.31
Unpaid labor	5.66	5.63	5.75
Total, economic costs	112.18	115.00	125.80
Residual returns to management and risk 7/	-44.06	-36.61	-26.43
Harvest-month price (dollars per bushel)	2.29	2.39	3.50
Yield (bushels per planted acre)	28.79	31.87	27.38

1/ Excludes direct effects of Government programs on costs and returns. 2/ Sum of operator and landlord costs and returns. 3/ Gross value of production less total cash expenses. 4/ Variable expenses multiplied by time between use and harvest and by 6-month U.S. Treasury bill rate. 5/ Value of machinery and equipment multiplied by longrun real rate of return to production assets in the farm sector. 6/ Rental value based on composite share and cash rent. 7/ Gross value of production less total economic costs.

Senator **Pryor**. Bruce, thank you. You are an economist. Right?

Mr. **Gardner**. Yes. I admit it. [Laughter.]

Senator **Pryor**. If you had to write a paper today, let's say, for your thesis, and the title of your thesis is: "Why Young People in America Should go Into Agriculture," what would the bottom line be? What would the thrust of that thesis be?

Mr. **Gardner**. Oh, I think I would base it on the notion that agriculture in the future is very likely to be a technically dynamic industry where managerial skills are going to be rewarded and that especially with the opening of world markets that we hope to achieve with the GATT negotiations that Senator Baucus was emphasizing, that this will be a very exciting time in the next 20 to 30 years to be in agriculture, and I think it is much better from every point of view than it was a few years ago to think about going into agriculture.

Senator **Pryor**. Now, if we open world markets and sell the products that are represented here in this room today, if we open those markets and sell everything that we produce, but if that farmer out there can't make a profit on it, what's going to happen?

Mr. **Gardner**. Then you're not going to see this dynamic industry that we are talking about. [Laughter.]

Senator **Pryor**. That is the point of this hearing. And I think you realize that.

Senator Baucus.

Senator **Baucus**. Thank you, Mr. Chairman.

Bruce, as you know, there are some experts who estimate that cost of production is going to rise dramatically in the 1990's for some crops. The Food and Agricultural Policy Research Institute at the University of Missouri, for example estimates that by the year 1999 the cost of producing wheat will increase 63 percent, oats will increase by 62 percent, the cost of barley production will increase by 64 percent, and the cost of producing the steer by that same date will increase 6 percent.

If those estimates are accurate, why shouldn't the 1990 farm bill include a provision indexing target prices to cost of production? It seems to me that we ought to have a better way for farmers to manage their risks so that they can very aggressively compete in world markets and yet, at the same time, make a decent living.

Mr. **Gardner**. Well, let me return, Senator Baucus, to your first statistics or projections.

Senator **Baucus**. Right.

Mr. **Gardner**. I think those would be based on the sort of notion we have now that the likely rate of inflation over the next 10 years will be in the neighborhood of 4 to 5 percent, perhaps. And if you take our input prices and project them over the next 10 years, this is the kind of result you're going to get if you compound those price increases and you'll get 50–60 percent increase over a 10-year period.

Now, that will not necessarily—and in the past has not—translate into cost of production increases, because at the same time while the input prices have gone up, we've gotten more efficient. We have gotten more out of each unit of input we use, at a rate for U.S. agriculture as a whole of about 2 percent a year. So that we haven't in the past seen costs of production rise as fast as those input prices will.

Senator **Baucus**. Well, that begs the issue.

Mr. **Gardner**. Well, that is the prelude to it.

Senator **Baucus**. That still begs the issue. We are talking about trying to get a little more certainty into agriculture so that we can cultivate the managerial talent we need to compete in the next decade and the next century.

Mr. **Gardner**. And I agree that you can get certainty increased by the provisions you make for target prices. It's not clear to me, though, that you really increase certainty by this indexing method. Of course, you can set a path for target prices as was done in the 1985 act.

Senator **Baucus**. But it helps, doesn't it?

Mr. **Gardner**. Well, in the 1985 act, of course, what we had was a schedule of target prices that were there independently of what happened to input prices. And of course that gave you certainty.

Senator **Baucus**. Scheduled to come down.

Mr. **Gardner**. Yes, that's right. But if we're talking about certainty, that does give you the notion.

Senator **Baucus**. We're talking about positive certainty, not negative certainty. [Laughter.]

Mr. **Gardner**. Of course, that's up to the Congress and the bill you write. But what I am saying is it seems to me that if you have a schedule of target prices you would like to see in mind, you can legislate those as such rather than tying them to a price index.

Senator **Baucus**. And if we're a little uncertain as to what those costs of production actually are going to be, doesn't it make more sense to have an indexing provision rather than writing into law what those target price levels will be?

Mr. **Gardner**. Well, first of all, it would help if we had absolute confidence that we have these costs of production numbers right and that we have included only the things that should be included and excluded only the things that should be excluded, and the particular problem being again land. What if land prices start to accelerate, as they did?

Senator **Baucus**. We can help you write that cost of production definition.

Mr. **Gardner**. Well, yes, you can, but I would be worried first of all, what would happen if you had land in it? Second, if you look at what cost of production means for agriculture as a whole, it's an average that pertains to the set of people we surveyed, which we think represents all of agriculture as a whole fairly well, but there is a tremendous variation in the costs of production in different farms.

And what we found in the most recent cost of production surveys, where we have enough precise data that we can get a distribution of cost of production on different types of farms, what you find is a very large portion, in most cases the majority, of production comes in at a cost less than our national average cost of production. That means if you try to keep your target price ahead of that average cost, you run the risk of providing a continual overincentive to produce on those most efficient farms.

And for that reason, it's not clear to me that you should set the target price to try to cover all the costs of the average farm in the United States. And the trouble is if you depart from that, how do you depart from it? It just seems to me again that you create more problems than you solve. And I think it's better, myself, to look out into the next few years as best you can make the judgments now and set those target prices.

Senator **BAUCUS**. Well, we don't have the time to go into this in major detail. But I just think we have to do a better job in addressing this squeeze that faces so many producers. When we write the bill I hope we come up with a solution that better addresses that problem.

Senator **PRYOR**. Good.

Senator **BAUCUS**. Thank you.

Senator **PRYOR**. Bruce, there are a lot of further comments and questions I know Senator Baucus and myself would like to make, but we are going to excuse you at this time in the interest of time. We do appreciate your coming.

Mr. **GARDNER**. Thank you.

Senator **PRYOR**. Especially at such short notice.

Our next witness is Mr. Harvey Joe Sanner, a soybean farmer from Des Arc, Arkansas. Mr. Sanner is also president of the American Agriculture Movement. We appreciate Mr. Sanner being here.

STATEMENT OF HARVEY JOE SANNER, SOYBEAN FARMER, DES ARC, AR

Mr. **SANNER**. Thank you, Senator.

John, my bag is not hardly as neat as yours, but I brought some goodies too.

INTRODUCTION

You know, there have been so many good statements already made here this morning and points about cost of production, what has happened to them, that I don't want to take a lot of your time, Senator. I will show these to you later.

But here is a grind rock, a simple bench grinding stone. It was bought 10 years ago by a friend of mine in Des Arc. I went back to the NAPA Annapolis store last week, same parts number. It cost a little over $5. Now it's $15.45. I have a hitch pin and a spark plug, and I could have brought you a lot of other good things to make the point, but I think it has been well made this morning. And I wanted to bring these up here because I am afraid if I didn't, the next time I ask him to gather me up some material he wouldn't do it.

Senator **PRYOR**. Thank you, Harvey Joe. We appreciate those displays.

Mr. **SANNER**. I am kind of glad my wife is not here today, because if she had stood here behind Mr. Gardner, she would have messed up her hairdo scratching her head and trying to figure out how higher target prices are going to be harmful to us and raise our production costs. I am pretty puzzled by some of his remarks, and I hope we get to talk to him a little more later on.

I have a statement. It is submitted for the record, and I won't read it, Senator.

Senator **Pryor**. Your full statement will be placed in the record.

Mr. **Sanner**. First of all, I want to thank you so very much for holding this hearing. I think it was absolutely necessary because we have had several groups on the Hill in the past few months testify that we did not need to index target prices, that we simply needed to freeze targets where they were or maintain the 1985 farm bill.

1985 FARM BILL IS A ROAD MAP FOR DISASTER

I guarantee you that is a road map for disaster if we maintain the 1985 farm bill as it is, with the income supports that we know we can't maintain due to Gramm-Rudman pressure. I don't know where we're going to find the money to index targets. I don't think we will need that much money if we index loan rates along with targets. We will have the savings we need to take care of the indexed targets.

Senator Bumpers told me the other day that we could drop off one B-2. He said, "The damn thing won't fly anyway." [Laughter.]

So, you know, those are his remarks, not mine. So we could take one of the B-2 bombers and go ahead and pay for all the farm programs we want.

I think Mr. Tull and the gentleman from Georgia made some excellent statements about cost of production. Anything I could say about that would probably be redundant.

GET SOYBEANS ON PAR WITH OTHER COMMODITIES

But I would say this to John, that on a 300-acre rice farm, that might have been a $15,000 profit last year, I know what our Arkansas farmers used it for. They used it to grow soybeans because they were far below the cost of production, far more than $15,000 below.

Hopefully, out of all this, that we can come with a decent soybean program in the 1990 farm bill. I think we have the absolute worst program on the Hill. You can't find a straight soybean farmer in Arkansas anymore. If he doesn't have a program crop of some type, he's been out of business long ago. That definitely needs to be addressed. That's one of the problems we have had with it for years and years, with the Soybean Association and the other advocates.

We have to recognize that there is a relationship between these commodities. And I understand you have already introduced a soybean bill. So, hopefully, we will see it get soybeans on par with the other commodities before this debate is over.

TARGET PRICES

It seems to me to even be concerned, as Mr. Gardner and USDA is, about target prices, that they are already admitting failure in their farm bill proposal. If market prices are going to rise with this tremendous new growth that we are going to see in markets out there, target prices won't be an issue. It doesn't seem to me that if we had faith in our farm bill, that this would even be an issue at all. And I am a little confused by him saying that it's going to lead to overproduction if we raise target prices. The people in the program are not responsible for the overproduction. To qualify for the target price protection, you have to reduce production. So I think he is a little confused about what target prices would actually do.

INDEXING

Another thing I have trouble with in opposition to indexing is that indexing also means lowering. If it's tied to cost of production, the cost of production comes down and then the target price will come down.

ON THE ISSUE OF WHAT DO YOU DO TO ONE COMMODITY AT THE EXPENSE OF THE OTHER

On the issue of what do you do to one commodity at the expense of the other, and I have as much sympathy for cattlemen probably as they do me as a soybean farmer. We have to recognize that grains and oilseeds are the base of the world's food supply. We develop a program for those commodities and then develop a program for the cattlemen, poultry industry, pork industry so they can survive within it. You can't reduce the price of grain artificially and over the long term benefit cattlemen.

Even though we are seeing cattle prices at a higher rate than they have been in some time, as the gentleman said, we are going through a cycle. We have shook out a tremendous amount of family feeders in this country with this below-cost-of-production grain that we had for years that caused a glut in the cattle industry.

A FALLACY

So to say that you can lower prices in grain and supplement or support these other industries without causing real problems in all the sectors I believe is a fallacy. It just can't be done. Quite frankly, we have been subsidizing the poultry industry and all the other grain-consuming industries for a long time with below-cost-of-production grain prices.

I appreciate your doing this, again, this hearing. I think it's so timely. I don't know if the mood is going to change between now and when the farm bill comes together, where there will be a chance to recognize these cost-of-production increases and the need for indexing.

There is a tremendous propaganda mill out there. Ours is not near as productive as USDA and the other people who are convinced that we simply need to lower prices and sell more.

GATT

As far as the GATT position, I think the U.S. position in GATT would probably be the most damaging to U.S. agriculture than any proposal I have heard. One thing I think, the cattle people I have talked with and I have sat in some seminars on decoupling, and the U.S. position is that we can go ahead and destroy these grain farmers and we can get rid of our programs, if that's what they want, and then we can all grow cows. [Laughter.]

That is what we will do on a lot of that land. You know, if we don't have a rice program and we don't have cotton programs and wheat programs, then we can grow cattle. Then we could all be in the same boat again.

If we develop the oilseed and grain program as what we need to do, then use export-import laws or whatever is necessary to get the cattle industry healthy.

All studies that I have seen on GATT indicate that there will be a substantially reduced farm income. I cannot understand for the life of me, it being the U.S. position, to knowingly—knowingly—support a position that is going to drive farm income lower, simply in the name of free trade. If they can find a study that shows otherwise, well, I need to see it.

But everything that I have read about it and can understand is it's going to lead to reduced farm income and it's going to cause more of what we have been concerned about in AAM since 1977, this concentration in farm numbers and land ownership that is absolutely destroying our rural communities. It is continuing. It is going to continue.

YOUNG PEOPLE ARE NOT ENTERING FARMING

And speaker after speaker this morning has said that farm people, young people are not entering farming. Our age is getting older. I go to a lot of farm meetings, and sometimes I am the youngest one there anymore. And I am 47. And it's kind of scary. We don't have any 25-, 22-, 24-, 25-year-old farmers entering agriculture. Very few. And that ought to be the real issue.

Now, if you wait until it impacts Mr. Gardner or it impacts USDA, there won't be any rural America left out there before we do something about it.

So that is the real issue I know that you're concerned about, and why you agreed to hold this hearing, and again I thank you for it. I have probably said all I need to say at this time.

[The prepared statement and attachments of Mr. Sanner follow:]

America Needs Parity!

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TESTIMONY OF

HARVEY JOE SANNER, NATIONAL PRESIDENT

AMERICAN AGRICULTURE MOVEMENT, INC.

before the

Subcommittee on
Agricultural Production and Stabilization of Price
Senate Committee on Agriculture, Nutrition, and Forestry

April 23, 1990

Thank you, Mr. Chairman. My name is Harvey Joe Sanner, and I appreciate the chance to be here today to offer American Agriculture Movement's views on costs of production.

On behalf of our members, let me begin by saying that costs of production are meaningless numbers unless compared to returns, and that we can think of no other industry besides agriculture in which producers are expected to receive less for a product at the point of sale than it cost them to produce it. Through the 1990 farm bill, we have a chance to change that -- to give producers the opportunity to earn their income from the marketplace instead of relying on the federal government to find money for subsidy payments while consumers enjoy the safest most plentiful food supply at the lowest cost in the world. I would like to thank you, Mr. Chairman, for the foresight you have shown by focusing attention on this issue here today.

The United States Department of Agriculture statistics attached to my testimony indicate very clearly that production costs have been increasing for most commodities, and that returns have not kept pace. In spite of claims by Secretary Yeutter and others that "all is well in agriculture", the slightest effort to dig below the surface reveals that the recovery is spotty, and favors commodities that do not have to live with a government program or where the government program is a properly-run supply management program. I hasten to add that in the latter category, the Administration has proposed changes for the 1990 farm bill that would push producers of peanuts, tobacco, and sugar into the same quicksand that has been swallowing up producers of wheat, feedgrains, cotton, rice, and dairy products throughout the last decade. Gains from lower livestock numbers and in fruits and vegetables account for much of the overall increase in total U.S. farm income.

Last month, the Food and Agriculture Policy Research Institute (FAPRI) issued its outlook for agriculture over the next eight years, assuming a basic continuation of the 1985 farm bill with target prices frozen at 1990 levels. FAPRI concluded that the picture for the early 1990's is about the same as today, but that in the late 1990's increases in production costs would outstrip yield increases while government payments continued to drop. The tables attached to my testimony show little good news for net farm income in the absence of a 1990 farm bill that changes direction by substantially increasing loan rates. Not insignificantly, the same action would greatly reduce the Commodity Credit Corporation's costs of doing business even as it enabled farmers to seek their full costs of production from the marketplace.

Let me emphasize full costs of production. Economic projections are full of footnotes indicating that cash costs don't include a particular item, or that labor costs don't count the value of the operator's time, or that interest on land payments isn't included, and the like. Let me assure you, Mr. Chairman, that to a farmer -- and even more so to his banker -- the operation needs to recover its total costs of production to stay in business. Income figures that leave out a particular cost factor, even for the sake of industry-wide generalizations, are masking the truth faced by many American farmers.

As examples, the dairy support price is now nearly $3.00 per hundredweight below USDA's estimate for the average full cost of production in 1988 ($10.60 versus $13.14). The current market price for manufacturing grade milk is about halfway between the two ($12.02). In other words, the best hope of a producer who is trying to purchase his farm is to start out in an area with a large percentage of fluid use, and therefore a better blend price. Frustratingly, only six years ago, the support price was $13.10 per hundredweight.

Similar stories exist for target prices in wheat and feedgrains. In fact, the only commodities that have seen market prices even close to the cost of production have been peanuts, tobacco, and sugar. In each of the years 1985 - 1987 Congress enacted major legislation to rescue the Farm Credit System, which held the lion's share of farm real estate loans. Mr. Chairman, I don't claim to have a Ph.D. in agricultural economics, but I do know how to put two and two together. Even today, many farmers are carrying debt, and to design farm programs as if that were not true is short-sighted.

Incomplete estimates of production costs also hide the inability of many farmers to pass their costs along the food chain. I'm sure you're familiar with the old saying that farmers buy at retail, but sell at wholesale. Just imagine how the saying will go when the rest of the livestock sector follows the contract farming trend set by the broiler industry 25 years ago -- "Farmers buy at retail and sell for whatever the completely integrated multinational corporations will give them." We are becoming less able to bargain with those from whom we buy and with those to whom we sell. When both of those parties are the same corporation, that is even more the case. When the corporation on the other side of the bargaining table holds a patent on the product the farmers wishes to buy, effectively there is no bargaining.

Agriculture, like many other industries, has seen a flood of new devices designed to save labor and lower the cost of doing business. This has been true for years in equipment, and lately in plant varieties. Now, biotechnology is bringing these same types of advances to livestock. Of course, the capital investment necessary to acquire these modern technological miracles is enormous, and grows each year, because the manufacturers want to be sure to recover their costs of production. Tractors and self-propelled machinery costs increased 91% from 1978 to 1988, according to USDA. Overall, the average cost of commodities, taxes, interest, and farm wage rates climbed 72% in the same period. By comparison, 1990 target prices are 20% higher for upland cotton than they were in 1980, 15% higher for corn than in 1980, 12% higher for rice than they were in 1980, 10% higher for wheat than in 1980, 4% higher for sorghum than they were in 1980, and 7.5% lower for barley than in 1980. When comparing the facts, i.e. a small increase in support levels versus a huge increase in costs, it's easy to see why so many of America's family farmers and ranchers still haven't gotten the word that the farm crisis is over.

Another cost that is rising because it is a less obvious "revenue raiser" than a straightforward income tax hike is excise taxes. Politicians know that excise taxes tend to be smaller and are therefore less objectionable to the person paying them each time, so we're seeing them proposed at higher levels on more commodities. But excise taxes add up quickly and regressively to raise farmers' costs of production. According to a recent study, the impact of excise taxes is 33% higher in rural areas than urban areas. Fuel is a major input for farming. Off the farm, rural Americans have to drive farther to get from place to place. We're more likely to have to place a toll call to reach anyone. We use tobacco products and beverages just like anyone else. The average consumer does not understand that the excise taxes he pays are also paid by the people producing his food, and that farmers are hit the hardest.

Consumers also fail to understand the bargain that food actually is in the United States. On average, the United Nations estimates that Americans spend only 10.4% of their income on food, compared to 16.8% in France, 28% in the USSR, and 62.9% in the Sudan. And the farmers' share of that 10.4% has been steadily declining.

Finally, there are some hidden costs of production that consumers and, too often, producers themselves haven't recognized. I am referring to the impact on the environment. In a struggle to make up in volume what they were not getting in value, many farmers have attempted to make ends meet by overdoing it on fertilizers and pesticides. Not only did this increase overall input costs, it also cost us soil fertility and water quality. Many farmers have cut back on purchased inputs, and several legislative proposals have already been introduced to help farmers wishing to use soil-restoring crop rotations and to increase water quality research and education. But producers and consumers must be made to understand that overproduction and a cheap food policy in the short term does have an impact on our resource base for the long term -- there is a cost, and the bill is already coming due. For example, many lenders already require water quality testing before agreeing to lend money to purchase a farm or to take a farm into inventory. Many communities are finding that their groundwater supplies have residues near or beyond the point of contamination. With more than 90% of rural residents relying on groundwater for their primary source of drinking water, this is another example of Rural America bearing the brunt of the cost.

What can be done to improve the relationship between cost of production and producer returns? Last month I appeared before the full Senate Committee on Agriculture, Nutrition, and Forestry to offer our recommendations for the 1990 farm bill. An outline of our proposal is attached to my testimony as Attachment C.

Mr. Chairman, thank you for the opportunity to testify today. I would be happy to answer any questions you might have.

United States
Department of
Agriculture

Economic
Research
Service

ECIFS 8-4

Economic Indicators of the Farm Sector

Costs of Production

Major Field Crops, 1988

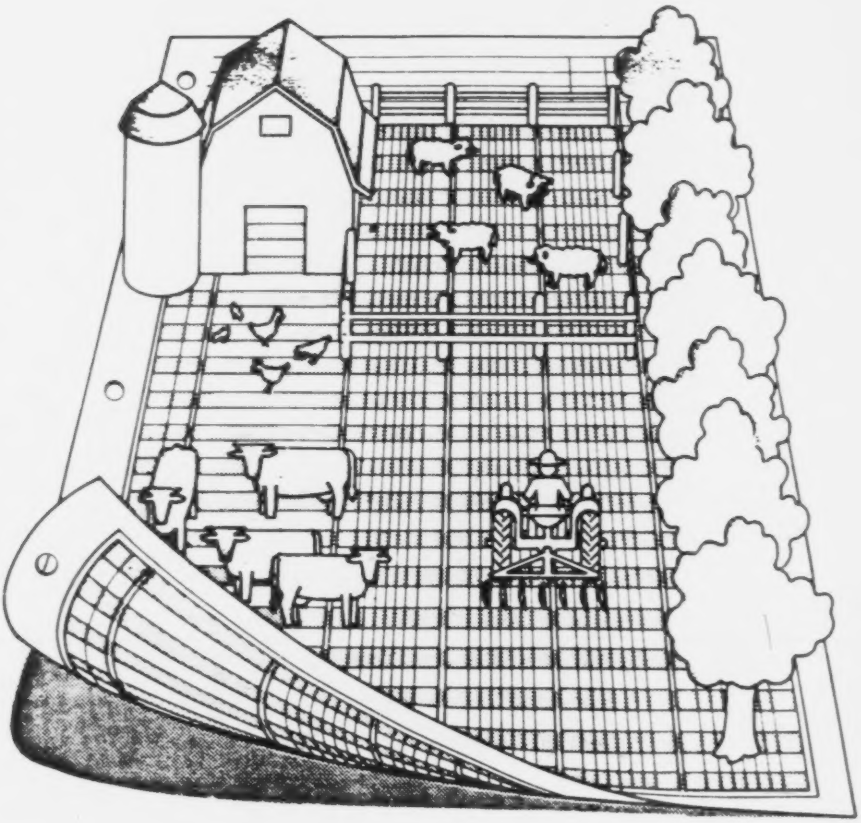

Table 71--U.S. barley production costs and returns per planted acre, 1975-88 1/, 2/

Year	Yield per planted acre 3/	Costs					Returns			
		Cash expenses			Cash expenses plus capital replacement	Total economic costs 4/	Gross value of production	Net returns after cash expenses	Net returns after cash expenses and capital replacement	Residual returns to risk and management 5/
		Variable	Fixed	Total						
	Bushels	Dollars								
1975	40.60	34.64	24.09	58.73	70.07	83.87	101.06	42.32	30.98	17.18
1976	41.30	32.92	24.17	57.09	70.11	83.84	96.53	39.44	26.42	12.69
1977	39.60	31.31	24.61	55.93	69.31	79.81	73.91	17.99	4.61	-5.90
1978	45.80	41.64	27.38	69.01	86.33	106.49	91.28	22.26	4.94	-15.21
1979	47.80	49.04	31.18	80.22	102.09	125.12	111.65	31.43	9.56	-13.47
1980	43.28	56.23	34.90	91.13	114.42	137.20	118.69	27.56	4.27	-18.51
1981	49.61	61.41	44.40	105.81	130.82	146.57	124.80	18.99	-6.02	-21.77
1982	53.44	64.67	35.71	100.38	124.09	148.21	117.65	17.27	-6.44	-30.56
1983	49.65	60.49	42.22	102.71	127.27	146.04	120.31	17.60	-6.96	-25.73
1984	50.46	64.40	35.96	101.61	126.55	143.80	119.27	17.66	-7.28	-24.53
1985	44.96	57.89	28.05	85.94	110.00	128.90	87.04	1.10	-22.96	-41.86
1986	46.83	53.51	27.97	81.48	105.89	135.23	71.23	-10.25	-34.66	-64.00
1987	47.42	50.30	24.60	74.90	98.51	132.07	82.26	7.36	-16.25	-49.81
1988	27.81	52.34	24.15	76.49	99.39	136.75	83.65	7.16	-15.74	-53.10

1/ Excludes direct effects of Government programs on costs and returns. 2/ Sum of operator and landlord costs and returns. 3/ Weighted average of States surveyed. 4/ Economic costs are cash expenses less interest paid plus capital replacement and allocated returns to operating capital, nonland capital, land, and unpaid labor. 5/ Gross value of production less total economic costs.

Table 72--U.S. corn production costs and returns per planted acre, 1975-88 1/, 2/

Year	Yield per planted acre 3/	Costs					Returns			
		Cash expenses			Cash expenses plus capital replacement	Total economic costs 4/	Gross value of production	Net returns after cash expenses	Net returns after cash expenses and capital replacement	Residual returns to risk and management 5/
		Variable	Fixed	Total						
	Bushels	Dollars								
1975	85.70	81.34	49.09	130.43	144.71	182.57	217.50	87.07	72.79	34.94
1976	87.10	77.69	49.64	127.34	144.97	178.24	187.11	59.78	42.15	8.88
1977	88.80	80.09	50.90	131.00	149.56	183.30	180.12	49.12	30.56	-3.18
1978	100.50	87.44	48.26	135.70	154.87	200.36	225.94	90.25	71.08	25.59
1979	109.60	99.94	53.84	153.78	176.78	238.07	275.97	122.19	99.19	37.90
1980	90.15	119.38	65.84	185.22	210.51	262.60	279.46	94.24	68.95	16.86
1981	109.28	135.09	72.28	207.37	235.38	278.60	260.17	52.80	24.79	-18.43
1982	113.76	133.52	77.44	210.96	244.21	270.86	243.63	32.67	-.58	-27.23
1983	78.76	128.30	73.77	202.07	235.63	258.45	252.90	50.83	17.27	-5.55
1984	105.79	132.34	78.28	210.62	244.35	287.96	273.23	62.61	28.88	-14.73
1985	117.29	136.81	61.12	197.93	232.55	277.02	252.63	54.70	20.08	-24.39
1986	118.46	120.41	45.19	165.60	195.37	243.12	167.60	2.00	-27.77	-75.52
1987	118.83	117.39	40.91	158.50	188.38	244.87	186.02	27.72	-2.36	-58.55
1988	83.15	122.22	40.36	162.58	193.59	262.58	216.39	53.81	22.80	-46.19

1/ Excludes direct effects of Government programs on costs and returns. 2/ Sum of operator and landlord costs and returns. 3/ Weighted average of States surveyed. 4/ Economic costs are cash expenses less interest paid plus capital replacement and allocated returns to operating capital, nonland capital, land, and unpaid labor. 5/ Gross value of production less total economic costs.

Table 73--U.S. cotton production costs and returns per planted acre, 1975-88 1/, 2/

Year	Yield per planted acre 3/	Costs					Returns			
		Cash expenses			Cash expenses plus capital replacement	Total economic costs 4/	Gross value of production	Net returns after cash expenses	Net returns after cash expenses and capital replacement	Residual returns to risk and management 5/
		Variable	Fixed	Total						
	Pounds	Dollars								
1975	416.00	141.08	37.23	178.31	209.56	234.53	252.40	74.00	42.84	17.87
1976	435.00	143.71	38.26	181.97	221.56	256.64	325.79	143.82	104.23	69.15
1977	505.00	160.73	40.09	200.82	241.92	276.78	314.09	113.27	72.17	37.31
1978	390.00	159.90	37.58	197.48	232.46	276.83	262.33	64.86	29.88	-14.49
1979	502.40	189.24	40.77	230.01	272.75	328.54	366.02	136.01	93.27	37.47
1980	367.19	200.34	40.97	241.31	287.54	338.18	313.78	72.47	26.24	-24.40
1981	523.88	216.25	83.75	300.00	338.21	359.73	325.55	25.55	-12.66	-34.18
1982	550.73	235.80	88.09	323.89	366.47	393.52	354.38	30.49	-12.09	-39.14
1983	470.40	224.92	87.29	312.21	357.09	386.84	377.05	64.84	19.96	-9.79
1984	554.65	229.51	89.61	319.12	363.18	389.20	365.25	46.13	2.07	-23.95
1985	598.35	245.50	77.59	323.09	368.66	404.50	363.86	40.77	-4.80	-40.64
1986	462.97	217.84	77.96	295.80	346.15	388.08	255.68	-40.12	-90.47	-132.40
1987	683.29	250.74	69.57	320.31	371.96	458.55	489.25	168.94	117.29	30.70
1988	594.94	249.36	68.04	317.40	371.99	454.06	381.31	63.91	9.32	-72.75

1/ Excludes direct effects of Government programs on costs and returns. 2/ Sum of operator and landlord costs and returns. 3/ Weighted average of States surveyed. 4/ Economic costs are cash expenses less interest paid plus capital replacement and allocated returns to operating capital, nonland capital, land, and unpaid labor. 5/ Gross value of production less total economic costs.

Table 74--U.S. flaxseed production costs and returns per planted acre, 1975-88 1/

Year	Yield per planted acre 2/	Costs					Returns			
		Cash expenses			Cash expenses plus capital replacement	Total economic costs 3/	Gross value of production	Net returns after cash expenses	Net returns after cash expenses and capital replacement	Residual returns to risk and management 4/
		Variable	Fixed	Total						
	Bushels	Dollars								
1975	9.10	17.96	16.45	34.40	44.22	56.48	59.31	24.91	15.09	2.84
1976	7.10	15.94	16.46	32.41	42.91	53.83	49.87	17.46	6.96	-3.96
1977	10.70	16.69	16.98	33.67	44.99	57.12	48.19	14.52	3.20	-8.92
1978	12.40	19.27	18.66	37.93	51.33	69.73	70.61	32.69	19.29	.88
1979	13.20	23.40	20.95	44.36	58.91	77.36	78.05	33.69	19.14	.69
1980	12.03	23.57	22.19	45.76	63.73	82.80	84.65	38.89	20.92	1.85
1981	12.09	30.46	23.95	54.41	72.35	92.92	79.63	25.22	7.28	-13.29
1982	13.21	36.80	22.34	59.14	80.05	101.02	78.10	18.96	-1.95	-22.92
1983	11.51	34.72	25.85	60.57	82.85	102.71	86.18	25.61	3.33	-16.53
1984	12.65	34.14	25.54	59.68	81.55	102.00	79.49	19.81	-2.06	-22.51
1985	13.37	34.07	21.40	55.47	77.79	98.63	82.24	26.77	4.45	-16.39
1986	16.03	29.36	18.56	47.92	70.36	91.19	64.25	16.33	-6.11	-26.94
1987	15.84	29.18	19.29	48.47	71.58	91.13	55.74	7.27	-15.84	-35.39
1988	5.88	27.79	15.71	43.50	64.38	83.75	48.20	4.70	-16.18	-35.55

1/ Sum of operator and landlord costs and returns. 2/ Weighted average of States surveyed. 3/ Economic costs are cash expenses less interest paid plus capital replacement and allocated returns to operating capital, nonland capital, land, and unpaid labor. 4/ Gross value of production less total economic costs.

Table 75--U.S. oats production costs and returns per planted acre, 1975-88 1/, 2/

Year	Yield per planted acre 3/	Costs					Returns			
		Cash expenses: Variable	Cash expenses: Fixed	Cash expenses: Total	Cash expenses plus capital replacement	Total economic costs 4/	Gross value of production	Net returns after cash expenses	Net returns after cash expenses and capital replacement	Residual returns to risk and management 5/
	Bushels	Dollars								
1975	43.60	22.94	16.55	39.49	48.40	61.78	90.83	51.34	42.43	29.05
1976	40.30	20.48	17.05	37.53	47.87	60.52	91.34	53.81	43.47	30.82
1977	53.80	23.55	17.58	41.13	52.59	66.92	95.12	53.98	42.52	28.20
1978	50.10	27.80	19.64	47.44	61.49	83.78	90.17	42.72	28.67	6.38
1979	50.90	32.49	22.28	54.77	70.02	96.08	87.70	32.93	17.68	-8.38
1980	49.92	40.10	27.50	67.60	84.20	107.28	101.52	33.92	17.32	-5.76
1981	52.84	44.35	35.04	79.39	97.78	119.76	121.37	41.98	23.59	1.61
1982	55.25	47.23	30.05	77.28	99.33	130.66	103.77	26.49	4.44	-26.89
1983	48.92	43.27	31.60	74.87	97.85	124.61	94.60	19.73	-3.25	-30.01
1984	50.82	45.24	33.56	78.80	102.22	131.33	104.74	25.98	2.52	-26.59
1985	45.14	41.85	29.12	70.97	90.14	112.04	79.43	8.46	-10.71	-32.61
1986	56.78	37.19	29.79	66.98	94.43	120.27	68.94	1.96	-25.49	-51.33
1987	53.98	39.83	35.53	75.36	102.95	129.11	93.23	17.87	-9.72	-35.88
1988	35.44	41.69	37.82	79.51	99.90	127.38	122.43	42.92	22.53	-4.95

1/ Excludes direct effects of Government programs on costs and returns. 2/ Sum of operator and landlord costs and returns. 3/ Weighted average of States surveyed. 4/ Economic costs are cash expenses less interest paid plus capital replacement and allocated returns to operating capital, nonland capital, land, and unpaid labor. 5/ Gross value of production less total economic costs.

Table 76--U.S. peanut production costs and returns per planted acre, 1975-88 1/

Year	Yield per planted acre 2/	Costs					Returns			
		Cash expenses: Variable	Cash expenses: Fixed	Cash expenses: Total	Cash expenses plus capital replacement	Total economic costs 3/	Gross value of production	Net returns after cash expenses	Net returns after cash expenses and capital replacement	Residual returns to risk and management 4/
	Pounds	Dollars								
1975	2,533.00	203.11	61.88	264.99	283.84	357.59	509.28	244.30	225.45	151.70
1976	2,445.00	199.33	61.60	260.94	282.64	357.98	503.01	242.07	220.37	145.03
1977	2,431.00	230.51	64.49	295.00	328.74	441.54	523.33	228.33	194.59	81.79
1978	2,602.00	246.82	68.04	314.85	349.57	468.49	561.46	246.61	211.89	92.97
1979	2,587.00	270.03	75.31	345.34	381.42	511.79	550.47	205.13	169.05	38.68
1980	1,526.43	287.27	73.72	360.99	400.01	517.96	376.45	15.46	-23.56	-141.51
1981	2,647.61	306.19	147.61	453.80	497.43	534.03	721.19	267.39	223.76	187.16
1982	2,642.50	292.32	133.93	426.25	473.13	505.20	667.41	241.16	194.28	162.21
1983	2,350.15	291.71	136.26	427.96	477.81	498.33	580.01	152.05	102.20	81.68
1984	2,827.78	307.29	113.47	420.76	470.28	521.36	726.46	305.70	256.18	205.10
1985	2,771.74	295.10	100.63	395.73	438.78	490.33	638.00	242.27	199.22	147.67
1986	2,354.78	274.11	112.97	387.08	435.50	597.65	689.78	302.70	254.28	92.13
1987	2,305.46	295.24	95.73	390.97	439.86	617.59	655.51	264.54	215.65	37.92
1988	2,402.36	297.61	93.59	391.20	442.71	633.30	662.65	271.45	219.94	29.35

1/ Sum of operator and landlord costs and returns. 2/ Weighted average of States surveyed. 3/ Economic costs are cash expenses less interest paid plus capital replacement and allocated returns to operating capital, nonland capital, land, and unpaid labor. 4/ Gross value of production less total economic costs.

Table 77--U.S. rice production costs and returns per planted acre, 1975-88 1/, 2/

Year	Yield per planted acre 3/	Costs					Returns			
		Cash expenses			Cash expenses plus capital replacement	Total economic costs 4/	Gross value of production	Net returns after cash expenses	Net returns after cash expenses and capital replacement	Residual returns to risk and management 5/
		Variable	Fixed	Total						
	Cwt.	Dollars								
1975	45.54	189.25	78.21	267.46	296.50	336.77	364.59	97.13	68.09	27.82
1976	46.79	185.84	77.74	263.58	290.44	323.01	314.93	51.35	24.49	-8.08
1977	43.99	171.06	78.98	250.03	278.85	322.94	400.26	150.23	121.41	77.32
1978	44.49	181.71	84.15	265.03	296.91	337.00	348.08	82.21	51.16	11.07
1979	45.70	201.64	92.30	293.94	331.02	396.30	460.07	166.14	129.06	63.78
1980	43.24	234.46	100.36	334.82	374.99	429.29	462.37	127.55	87.40	33.08
1981	47.75	258.27	97.11	355.38	398.32	460.86	487.67	132.29	89.35	26.81
1982	46.86	272.55	91.59	364.14	409.41	435.99	356.65	-7.49	-52.76	-79.34
1983	45.53	268.39	82.93	351.32	399.26	443.42	400.12	48.80	.86	-43.30
1984	48.87	255.20	89.95	345.15	394.86	438.80	393.22	48.07	-1.64	-46.58
1985	53.78	271.41	91.69	363.10	430.71	472.21	430.71	67.61	16.17	-41.50
1986	56.97	287.21	67.11	354.32	395.01	421.36	218.41	-135.91	-176.60	-202.95
1987	54.67	285.19	58.35	343.54	387.81	434.06	263.89	-79.65	-123.92	-170.17
1988	54.61	296.09	57.09	353.18	399.52	475.14	370.33	17.15	-29.19	-104.81

1/ Excludes direct effects of Government programs on costs and returns. 2/ Sum of operator and landlord costs and returns. 3/ Weighted average of States surveyed. 4/ Economic costs are cash expenses less interest paid plus capital replacement and allocated returns to operating capital, nonland capital, land, and unpaid labor. 5/ Gross value of production less total economic costs.

Table 78--U.S. grain sorghum production costs and returns per planted acre, 1975-88 1/, 2/

Year	Yield per planted acre 3/	Costs					Returns			
		Cash expenses			Cash expenses plus capital replacement	Total economic costs 4/	Gross value of production	Net returns after cash expenses	Net returns after cash expenses and capital replacement	Residual returns to risk and management 5/
		Variable	Fixed	Total						
	Bushels	Dollars								
1975	45.80	41.07	22.57	63.64	77.73	100.25	108.91	45.26	31.17	8.66
1976	46.00	36.78	22.50	59.28	76.54	96.95	93.69	34.41	17.15	-3.26
1977	54.10	40.49	23.31	63.80	81.71	104.13	98.79	34.99	17.08	-5.34
1978	53.20	43.02	24.66	67.68	86.26	110.67	152.12	84.44	65.86	41.46
1979	61.40	51.42	27.20	78.62	101.23	135.78	144.15	65.54	42.93	8.38
1980	43.16	58.26	30.22	88.48	114.15	145.27	131.17	42.69	17.02	14.10
1981	62.95	67.44	40.94	108.38	135.64	162.82	141.50	33.12	5.86	-21.32
1982	57.64	69.16	37.75	106.91	130.78	154.74	121.36	14.45	-9.42	-33.38
1983	46.29	66.76	36.23	102.99	129.73	157.00	131.58	28.59	1.85	-25.42
1984	52.81	64.40	35.96	100.36	124.29	149.08	123.73	23.37	-.56	-25.35
1985	65.89	62.61	26.89	89.50	112.06	147.98	124.99	35.49	12.93	-22.99
1986	66.91	55.50	25.39	80.89	103.93	133.66	91.57	10.68	-12.36	-42.09
1987	68.62	55.70	26.47	82.17	105.30	136.54	96.18	14.01	-9.12	-40.36
1988	62.13	56.88	31.92	88.80	112.71	155.05	148.43	59.63	35.72	-6.62

1/ Excludes direct effects of Government programs on costs and returns. 2/ Sum of operator and landlord costs and returns. 3/ Weighted average of States surveyed. 4/ Economic costs are cash expenses less interest paid plus capital replacement and allocated returns to operating capital, nonland capital, land, and unpaid labor. 5/ Gross value of production less total economic costs.

Table 79--U.S. soybean production costs and returns per planted acre, 1975-88 1/

Year	Yield per planted acre 2/	Costs					Returns			
		Cash expenses			Cash expenses plus capital replacement	Total economic costs 3/	Gross value of production	Net returns after cash expenses	Net returns after cash expenses and capital replacement	Residual returns to risk and management 4/
		Variable	Fixed	Total						
	Bushels	Dollars								
1975	28.30	38.23	30.50	68.73	82.15	118.80	139.93	71.19	57.77	21.12
1976	25.20	34.88	30.60	65.48	80.66	127.95	172.46	106.98	91.80	44.51
1977	30.20	41.23	31.36	72.58	88.86	140.55	178.46	105.87	89.59	37.90
1978	29.20	44.81	33.57	78.39	94.82	153.78	195.43	117.05	100.62	41.66
1979	31.90	50.58	36.72	87.30	105.92	166.27	201.32	114.03	95.41	35.05
1980	25.86	56.38	43.48	99.86	119.23	179.89	199.71	99.85	80.48	19.82
1981	29.68	62.52	46.42	108.94	129.53	178.79	179.48	70.54	49.95	.69
1982	31.32	61.38	46.51	107.89	131.05	172.02	160.64	52.75	29.59	-11.38
1983	25.72	59.61	54.18	113.79	138.29	183.81	204.46	90.67	66.17	20.65
1984	27.54	60.71	56.57	117.28	141.45	174.97	166.72	49.44	25.27	-8.25
1985	34.17	56.68	40.02	96.70	126.30	170.07	165.96	69.26	39.66	-4.11
1986	32.94	49.08	39.49	88.57	120.05	161.21	150.64	62.07	30.59	-10.57
1987	33.83	51.04	43.77	94.81	126.65	170.01	171.66	76.85	45.01	1.65
1988	26.60	54.17	45.84	100.01	134.02	185.86	200.25	100.24	66.23	14.39

1/ Sum of operator and landlord costs and returns. 2/ Weighted average of States surveyed. 3/ Economic costs are cash expenses less interest paid plus capital replacement and allocated returns to operating capital, nonland capital, land, and unpaid labor. 4/ Gross value of production less total economic costs.

Table 80--U.S. sugar-beet production costs and returns per planted acre, 1981-88 1/

Year	Yield per planted acre 2/	Costs					Returns			
		Cash expenses			Cash expenses plus capital replacement	Total economic costs 3/	Gross value of production	Net returns after cash expenses	Net returns after cash expenses and capital replacement	Residual returns to risk and management 4/
		Variable	Fixed	Total						
	Tons	Dollars								
1981	21.99	316.44	171.13	487.57	538.48	580.76	649.30	161.73	110.82	68.54
1982	19.83	307.76	128.10	435.86	489.47	593.42	704.96	269.10	215.49	111.54
1983	19.41	313.54	126.91	440.45	497.20	605.39	721.33	280.88	224.13	115.94
1984	19.68	286.28	135.85	422.13	480.32	575.57	668.02	245.89	187.69	92.45
1985	19.91	286.81	132.32	419.14	479.21	574.93	675.01	255.87	195.80	100.08
1986	20.39	274.22	136.44	410.66	470.59	574.85	731.88	321.22	261.29	157.03
1987	22.30	274.84	148.74	423.58	484.03	592.08	852.81	429.23	368.78	260.73
1988	19.19	378.16	149.09	527.25	593.84	734.86	787.98	260.73	194.14	53.12

1/ Sum of operator and landlord costs and returns. 2/ Weighted average of States surveyed. 3/ Economic costs are cash expenses less interest paid plus capital replacement and allocated returns to operating capital, nonland capital, land, and unpaid labor. 4/ Gross value of production less total economic costs.

Table 81--U.S. sugarcane production costs and returns per harvested acre, 1981-88 1/

Year	Yield per harvested acre 2/	Costs					Returns			
		Cash expenses			Cash expenses plus capital replacement	Total economic costs 3/	Gross value of production	Net returns after cash expenses	Net returns after cash expenses and capital replacement	Residual returns to risk and management 4/
		Variable	Fixed	Total						
	Tons	Dollars								
1981	36.60	684.87	100.56	785.43	846.68	1,131.15	922.68	137.25	76.00	-208.47
1982	39.60	737.08	103.76	840.84	906.63	1,183.53	1,061.43	220.59	154.80	-122.10
1983	37.30	725.97	105.23	831.20	899.51	1,154.87	1,050.20	219.00	150.69	-104.67
1984	37.30	712.43	107.30	819.73	897.54	1,149.27	1,058.82	239.09	161.28	-90.45
1985	37.10	712.43	107.30	775.94	852.53	1,095.09	998.68	222.74	146.15	-96.41
1986	30.90	476.78	86.42	563.20	626.15	838.10	828.12	264.92	201.97	-9.98
1987	28.70	461.72	85.04	546.77	610.45	824.34	858.13	311.36	247.69	33.79
1988	29.20	492.95	103.19	596.14	642.32	833.51	870.16	274.02	227.85	36.65

1/ Sum of operator and landlord costs and returns. 2/ Weighted average of States surveyed. 3/ Economic costs are cash expenses less interest paid plus capital replacement and allocated returns to operating capital, nonland capital, land, and unpaid labor. 4/ Gross value of production less total economic costs.

Table 82--U.S. sunflower production costs and returns per planted acre, 1979-88 1/

Year	Yield per planted acre 2/	Costs					Returns			
		Cash expenses			Cash expenses plus capital replacement	Total economic costs 3/	Gross value of production	Net returns after cash expenses	Net returns after cash expenses and capital replacement	Residual returns to risk and management 4/
		Variable	Fixed	Total						
	Cwt.	Dollars								
1979	13.20	38.99	22.73	61.72	78.28	108.40	116.55	54.83	38.27	8.15
1980	9.61	45.11	23.48	68.59	86.49	113.84	100.01	31.42	13.52	-13.83
1981	11.62	49.64	33.98	83.62	104.60	129.51	119.46	35.84	14.86	-10.05
1982	11.04	52.68	27.26	79.94	99.67	123.10	96.67	16.73	-2.43	-26.43
1983	10.28	53.16	37.73	90.89	110.75	130.20	125.74	34.85	14.99	-4.46
1984	9.95	52.03	37.06	89.09	107.53	127.31	115.38	26.29	7.85	-11.93
1985	10.26	48.83	24.22	73.05	91.36	117.73	108.11	35.06	16.75	-9.62
1986	13.23	46.58	23.24	69.82	88.82	114.20	97.72	27.90	8.90	-16.48
1987	14.47	47.15	26.64	73.79	92.71	116.10	98.37	24.58	5.66	-17.73
1988	8.33	45.87	23.98	69.85	88.87	116.04	102.92	33.07	14.05	-13.02

1/ Sum of operator and landlord costs and returns. 2/ Weighted average of States surveyed. 3/ Economic costs are cash expenses less interest paid plus capital replacement and allocated returns to operating capital, nonland capital, land, and unpaid labor. 4/ Gross value of production less total economic costs.

Table 83--U.S. wheat production costs and returns per planted acre, 1975-88 1/, 2/

Year	Yield per planted acre 3/	Costs					Returns			
		Cash expenses			Cash expenses plus capital replacement	Total economic costs 4/	Gross value of production	Net returns after cash expenses	Net returns after cash expenses and capital replacement	Residual returns to risk and management 5/
		Variable	Fixed	Total						
	Bushels	Dollars								
1975	28.50	32.59	20.69	53.28	63.74	84.81	104.39	51.10	40.64	19.58
1976	27.10	30.82	20.99	51.81	63.54	78.95	77.46	25.65	13.92	-1.49
1977	27.70	28.83	21.62	50.45	62.94	76.82	67.88	17.43	4.94	-8.94
1978	29.90	30.19	23.31	53.50	68.14	102.21	91.84	38.34	23.70	-10.37
1979	32.40	37.01	25.97	62.97	79.84	113.33	124.86	61.89	45.02	11.53
1980	29.87	46.76	28.99	75.75	93.90	122.25	116.48	40.73	22.58	-5.77
1981	31.47	55.25	34.59	89.88	109.18	132.85	118.96	29.08	9.78	-13.89
1982	32.64	56.03	32.46	88.49	107.90	132.25	114.69	26.20	6.79	-17.56
1983	36.89	56.77	37.60	94.37	115.39	140.78	132.97	38.60	17.58	-7.81
1984	33.79	54.61	39.46	94.07	114.55	134.36	118.45	24.38	3.90	-15.91
1985	31.41	51.10	25.23	76.33	95.96	125.26	96.00	19.67	.04	-29.26
1986	28.79	45.67	21.69	67.36	87.26	112.18	68.12	.76	-19.14	-44.06
1987	31.87	44.30	24.21	68.51	88.84	115.00	78.39	9.88	-10.45	-36.61
1988	27.38	46.63	24.54	71.17	91.74	125.80	99.37	28.20	7.63	-26.43

1/ Excludes direct effects of Government programs on costs and returns. 2/ Sum of operator and landlord costs and returns. 3/ Weighted average of States surveyed. 4/ Economic costs are cash expenses less interest paid plus capital replacement and allocated returns to operating capital, nonland capital, land, and unpaid labor. 5/ Gross value of production less total economic costs.

Appendix table 1--Indexes of prices paid by farmers, 1985-88

Index	1985	1986	1987	1988
		1977 = 100		
Prices paid by farmers for commodities and services, interest, taxes, and wage rates	162	159	161	170
Production items	151	144	147	157
Feed	116	108	103	128
Feeder livestock	154	153	179	192
Seed	153	148	148	150
Fertilizer	135	124	118	130
Agricultural chemicals	128	127	124	126
Fuels and energy	201	162	161	163
Farm and motor supplies	146	144	145	148
Autos and trucks	193	198	208	215
Tractors and self-propelled machinery	178	174	174	181
Other machinery	183	182	185	197
Building and fencing	136	136	137	138
Farm services and cash rent	150	145	146	147
Interest	228	211	190	186
Taxes	136	138	139	142
Wage rates	154	160	167	172
Production items, interest, taxes, and wage rates	156	150	151	160
		Percent		
Ratio of index of prices received by farmers to index of prices paid, interest, taxes, and wage rates	79	77	78	81

Source: Agricultural Prices, 1988 Summary.

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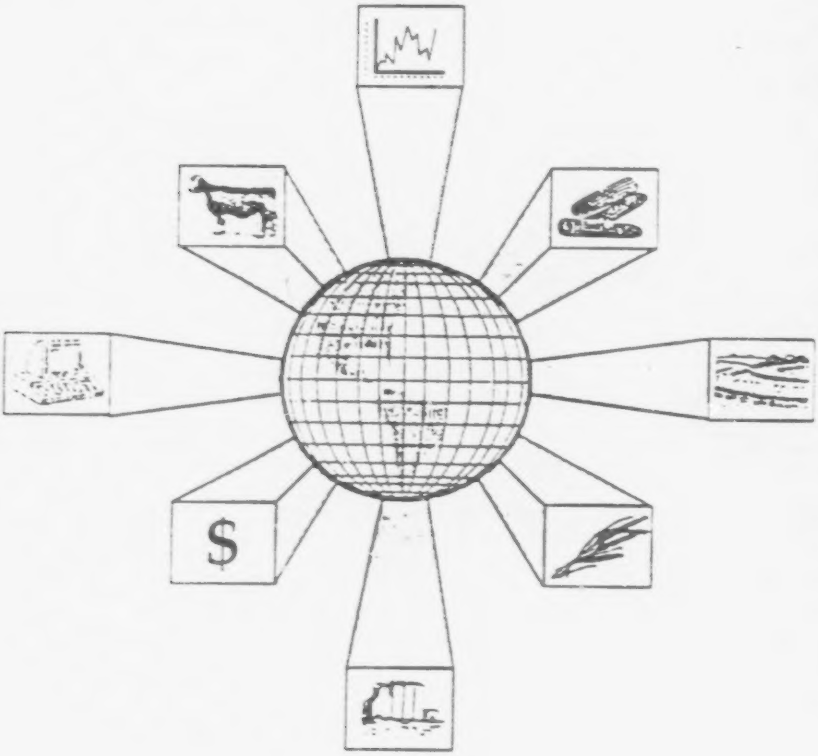
1990 U.S.
Agricultural Outlook

Staff Report #1-90
March 1990



Food and Agricultural Policy Research Institute
Iowa State University
University of Missouri- Columbia

Cash Receipts from Farming

Variable/Year	1987	1988	1989	1990	1991	1992	1993	1994		95-96 Avg
	....	....	....	(Billion Dollars)		....	....	....		....
Farm Marketings & CCC Loans	139.47	151.43	157.59	158.71	161.84	165.39	168.08	171.36	•	184.65
CROPS	63.75	72.57	74.76	76.26	78.82	82.31	83.63	85.83	•	94.68
Feed Grains	13.10	15.29	16.83	16.97	16.73	17.08	16.96	17.08	•	18.45
Corn	8.54	10.14	10.73	11.61	11.53	11.83	11.63	11.67	•	12.71
Sorghum	1.04	1.13	1.24	1.24	1.26	1.29	1.30	1.31	•	1.38
Barley	0.77	0.85	0.99	0.79	0.80	0.82	0.83	0.85	•	0.93
Oats	0.26	0.26	0.26	0.27	0.28	0.28	0.28	0.28	•	0.30
Hay	2.49	2.90	3.60	3.06	2.87	2.87	2.92	2.97	•	3.14
Food Grains	5.58	7.70	8.25	8.65	8.93	9.36	9.53	9.80	•	11.10
Wheat	4.97	6.43	7.09	7.46	7.76	8.23	8.37	8.62	•	9.81
Rice	0.58	1.25	1.15	1.17	1.15	1.10	1.13	1.16	•	1.26
Rye	0.03	0.02	0.02	0.02	0.02	0.02	0.02	0.02	•	0.02
Oilseeds	11.16	13.70	11.89	10.73	11.86	12.86	12.56	12.65	•	14.07
Cotton (Lint & Seed)	4.09	4.67	4.52	4.87	5.10	5.04	5.18	5.33	•	5.89
Other*	29.82	31.21	33.46	35.05	36.39	37.96	39.41	40.96	•	45.16
LIVESTOCK & PRODUCTS	75.72	78.86	82.84	82.44	83.02	83.08	84.45	85.53	•	89.97
Red Meats	44.28	45.98	46.62	47.08	46.93	46.20	46.36	46.45	•	48.37
Cattle & Calves	33.44	36.29	36.80	37.02	36.93	36.60	36.52	36.33	•	37.94
Hogs	10.29	9.21	9.22	9.46	9.39	9.01	9.24	9.53	•	9.83
Sheep & Lambs	0.54	0.47	0.60	0.60	0.60	0.60	0.60	0.60	•	0.60
Dairy Products	17.71	17.67	19.42	19.34	18.62	19.27	20.09	21.01	•	22.56
Poultry & Eggs	11.48	12.86	14.40	14.64	15.07	15.20	15.55	15.59	•	16.43
Broilers	6.18	7.43	8.07	8.32	8.78	8.85	9.25	9.17	•	9.81
Turkeys	1.70	1.95	2.20	2.15	2.25	2.25	2.35	2.35	•	2.42
Chicken Eggs	3.18	3.06	3.70	3.64	3.51	3.57	3.40	3.52	•	3.61
Other Poultry	0.42	0.42	0.42	0.53	0.54	0.54	0.56	0.56	•	0.58
Other Livestock**	2.25	2.36	2.40	2.38	2.40	2.40	2.44	2.48	•	2.61
GOVERNMENT PAYMENTS	16.75	14.48	10.76	8.65	9.82	9.96	10.07	9.89	•	7.91
TOTAL CASH RECEIPTS	156.22	165.91	168.35	167.36	171.66	175.34	178.15	181.25	•	192.56

*Includes tobacco, vegetables & melons, fruits & tree nuts, and other crops.

**Includes horses, mules, and aquaculture.

Farm Production Expenses

	1987	1988	1989	1990	1991	1992	1993	1994		95-98 Avg
				(Billion Dollars)						
Farm-origin Inputs:	33.75	38.41	41.26	38.34	37.86	38.66	38.34	37.85	•	39.91
Feed	18.90	22.46	24.41	21.55	20.97	21.88	21.53	21.10	•	22.30
Purchased Livestock	11.85	12.81	13.02	12.99	12.94	12.70	12.59	12.39	•	12.74
Seed	3.01	3.14	3.83	3.80	3.94	4.07	4.21	4.37	•	4.87
Manufactured Inputs:	18.23	19.43	21.91	22.08	21.79	22.37	23.51	24.64	•	28.45
Fertilizer & Lime	6.21	7.00	7.76	7.83	7.51	7.58	7.89	8.15	•	9.11
Petroleum Fuel & Oils	5.04	5.14	6.19	6.20	6.28	6.57	6.91	7.25	•	8.55
Electricity	2.39	2.57	2.86	2.83	2.97	3.16	3.33	3.57	•	4.29
Pesticides	4.59	4.72	5.10	5.23	5.03	5.07	5.38	5.67	•	6.51
Total Interest Charges:	15.49	15.17	14.71	15.39	16.09	16.30	16.38	17.04	•	18.58
Short-Term Interest	7.31	7.29	7.72	8.06	8.27	8.24	8.38	8.86	•	9.55
Real Estate Interest	8.19	7.89	7.00	7.33	7.82	8.06	8.00	8.17	•	9.03
Other Operating Expenses:	31.45	32.32	33.79	35.57	36.59	38.09	39.51	40.84	•	45.32
Repair & Operation of Capital Items	6.55	6.86	7.32	7.63	7.75	8.06	8.36	8.58	•	9.52
Contract & Hired Labor	10.82	11.20	11.37	11.65	11.95	12.23	12.60	12.97	•	14.25
Machine Hire & Custom Work	1.96	2.17	2.24	2.29	2.36	2.44	2.50	2.56	•	2.79
Marketing storage & transportation	3.82	3.28	3.67	4.28	4.23	4.40	4.47	4.53	•	4.88
Miscellaneous	8.31	8.81	9.18	9.70	10.31	10.96	11.58	12.19	•	14.07
Other Overhead Expenses:	29.07	29.63	29.79	30.43	30.60	31.46	32.94	33.98	•	36.95
Capital Consumption	17.66	17.72	17.81	18.29	18.16	18.57	19.74	20.46	•	22.32
Property Taxes	4.34	4.38	4.44	4.53	4.69	4.91	5.06	5.22	•	5.68
Rent to Nonoperators	7.06	7.53	7.54	7.61	7.76	7.98	8.14	8.31	•	8.95
Production Expenses:	128.00	134.96	141.46	141.82	142.93	146.88	150.67	154.36	•	169.22
Cash*	109.83	116.75	123.16	123.04	124.28	127.82	130.44	133.41	•	146.41
Cost of Op. Dwelling	2.29	2.37	2.41	2.40	2.43	2.50	2.55	2.60	•	2.70
Excluding Op. Dwelling	107.53	114.38	120.75	120.64	121.85	125.32	127.89	130.82	•	143.71
Noncash*	18.17	18.21	18.30	18.78	18.65	19.06	20.23	20.95	•	22.81
Capital Consumption	17.66	17.72	17.81	18.29	18.16	18.57	19.74	20.46	•	22.32
Perquisites to Hired Labor	0.51	0.49	0.49	0.49	0.49	0.49	0.49	0.49	•	0.49

*Includes cost of operator dwelling

Net Farm Income

	1987	1988	1989	1990	1991	1992	1993	1994		95-98 Avg
	....	....		(Billion Dollars)		....	....	....		....
1. Farm Receipts	145.28	157.10	163.47	164.80	168.14	171.87	174.80	178.34	*	192.35
Crops	63.75	72.57	74.76	76.26	78.82	82.31	83.63	85.83	*	94.68
Livestock	75.72	78.86	82.84	82.44	83.02	83.08	84.45	85.53	*	89.97
Farm-related*	5.81	5.67	5.88	6.09	6.29	6.48	6.73	6.98	*	7.70
2. Government Payments	16.75	14.48	10.76	8.65	9.82	9.96	10.07	9.89	*	7.91
3. Gross Cash Income (1+2)	162.02	171.58	174.23	173.45	177.95	181.83	184.87	188.23	*	200.26
4. Nonmoney Income	9.96	10.32	10.24	10.17	10.37	10.80	11.16	11.51	*	12.44
5. Value of Inventory Change	-0.36	-4.27	5.00	1.98	0.01	-0.32	-0.29	-0.04	*	0.38
6. Gross Farm Income (3+4+5)	171.63	177.63	189.47	185.60	188.33	192.31	195.74	199.71	*	213.08
7. Cash Expenses**	107.53	114.38	120.75	120.64	121.85	125.32	127.89	130.82	*	143.71
8. Total Expenses	128.00	134.86	141.46	141.82	142.93	146.88	150.67	154.36	*	169.22
9. Net Cash Income (3-7)	54.49	57.20	53.47	52.81	56.10	56.51	56.98	57.42	*	56.55
10. Net Farm Income (6-8)	43.63	42.86	48.01	43.78	45.40	45.43	45.06	45.35	*	43.85
Deflated (1982$)***	42.43	39.89	42.68	38.27	38.50	37.12	35.60	34.40	*	30.26

*Income from machine hire, custom work, sales of forest products, and other miscellaneous cash sources.

**Excludes capital consumption, perquisites to hired labor, & farm household expenses.

***Deflated by the prices paid index, all items, 1982=100.

Senator PRYOR. All right. Joe, let me ask you three questions.

Mr. SANNER. Yes.

Senator PRYOR. One, you are a soybean farmer. I see the soybean production costs up here on the table here.

Mr. SANNER. Yes, sir.

Senator PRYOR. All the way up to your right. We have had a discussion about those figures this morning.

Did you as a soybean farmer experience a cost of production decrease in the mid-1980's?

Mr. SANNER. Very slightly. Like the gentleman said, fuel costs did go down somewhat. Fertilizer did go down somewhat. And I think it was Mr. Kline that pointed out that this is a per-acre, not a per-bushel, figure we're looking at, and people did cut back on inputs. They were forced to. Many of them didn't have the money to put a crop in the ground.

So you know that chart may have some validity, but again it didn't put anybody on top of the world again by seeing that slight decrease. And what we have seen since is it's come back up.

Senator PRYOR. All right. In 1986 the USDA figure shows now increase of cost of production is escalating rapidly. Are you experiencing this in your operation?

Mr. SANNER. Yes. Yes.

Senator PRYOR. All right.

Mr. SANNER. All operations are, I think, Senator. And you know, you don't have to be an Einstein to look out in the country and see what happened to our farm debt, what happened to FmHA, the Farm Credit System, all of those. It's a result of these target prices and loan rates being too low.

USDA lied to you folks in Congress in 1985 when they used it as an excuse to come up here and drive support rates down when they knew darn well it was a lie. John Block had money he could have spent and moved exports into the world market. They had money last year they could have spent and they didn't. And they used that as an excuse to get rid of programs because they are antiprogram.

Senator PRYOR. All right. Speaking of programs, what would happen, what good or bad effects would happen, let's say, to the soybean farmer out there if we removed cross compliance, if they just did away with it?

Mr. SANNER. I don't think we need to do that. I think you would encourage quite a bit of soybean production. I think there is already, what amendments I have seen thus far, there is quite a bit of flexibility in the new farm bill, and I think it will correct the problems we have had with crop rotation and the other things that we have suffered due to cross compliance. So I don't think it would be a good idea to remove it right now, really.

Senator PRYOR. OK. A final question: What about the wetlands issue?

Mr. SANNER. Probably the hottest topic in the country right now. Everywhere I go in all the States, farmers are upset about it all over. It's so complex. We've got four different agencies telling farmers what they should be doing with their land, and I have talked to experts in the field who tell me they can't develop a definition of a wetland.

So it's going to take something pretty broad and sweeping, legislation like you have talked about and Congressman Alexander on the House side has introduced, that basically exempts farmland or land that had been farmed for the last 10 years from the wetland provision.

It is a hot topic. I might say we are as concerned about wetlands and the environment as anyone else, but we have gone too far. I think you used the term "Frankenstein" a while back that we had created with this no-net-loss program.

Another thing we've seen is definitely an implementation or, I would say, a discrimination against farm people over wetland, over potholes. We have developers all over the country building condominiums on wetlands, pushing down trees and draining swamps and doing all those sorts of things. But we have had a double standard, and maybe this legislation that you have been working on will take care of that problem.

Senator PRYOR. I want to thank you for your participation.

Mr. SANNER. Yes, sir. I appreciate being here.

Senator PRYOR. Thank you very much. Hope you will stay for lunch.

Mr. SANNER. Oh, I intend to.

Senator PRYOR. Good.

Mr. SANNER. That's the main reason I came.

Senator PRYOR. Good. Thank you, Harvey Joe.

Mr. Wiley Felty, wheat farmer from Altus, Oklahoma, our neighbor from Oklahoma.

Mr. Felty, we appreciate your being here this morning.

STATEMENT OF WILEY D. FELTY, WHEAT FARMER, ALTUS, OK

Mr. FELTY. Well, I appreciate the opportunity, Senator Pryor.

INTRODUCTION

I am Wiley Felty from Altus, Oklahoma, down in the southwest corner. With my father and my son, we raise cotton, wheat, and stocker cattle.

Mr. Kline has done a good job on the cotton deal today, so I will not dwell on that. I will apologize because I have about 17 pages, and being toward the tail end of testimony, I keep scratching this out and this out and this out.

Senator PRYOR. We will take your entire statement and have it printed in the record, should you desire.

Mr. FELTY. Well, right there is all I wrote down. I think I can talk good sense. [Laughter.]

Senator PRYOR. Good. Thank you.

OPERATING INPUT EXPENSES

Mr. FELTY. On the wheat production in Jackson County, Oklahoma, the average yield is between 26 and 27 bushels per acre. I have some operating input expenses developed by the agriculture economic department at Oklahoma State University, and I could make some minor changes by tinkering with it, but basically they came up with an $80.57 out-of-pocket cost per acre to plant, produce, and harvest.

They used custom harvesting and custom hauling on this, and probably it's a pretty good deal because there are more broke custom combiners than there are broke wheat farmers, and they're legends of both.

Using that 27-bushel average with interest cost of $9.15 per acre and depreciation, taxes, and insurance as the fixed cost of $10.60 per acre, and it also included rent. In my own mind, I cannot separate the cost of land from the cost of production, because if you own it and you're not getting the same return you would if you were renting it to somebody else, there's a bad false economy there.

The general rental is one-third in southwest Oklahoma grain crops. I figured two prices with the 27-bushel average, one at $3.50 and the other at $3 per bushel. And also, we graze Winter wheat pasture. I took an average of 130 pounds gain per acre on that, which added $42.90 per acre. So the productivity or the total income off of that wheat at the $3.50 level, 27-bushel growth value is $94.50. Add the $42.90 on it, that's a gross income of $137.40 per acre. You take the rent out, you take your fixed operating costs and your fixed costs out, that's $2.18 per acre profit without the Government program. Figure the $3.50 rate plus program payments in and you come up with $18.77 total above fixed cost.

Senator PRYOR. That is with the Government program?

Mr. FELTY. That's with the program. That doesn't include any return for management. It includes the labor for putting it in. It's less than most of us would care to work for. $4.50 an hour I believe is the figure that was used, and if you figured it at the $3 per bushel, which we have seen some of in the last 2 years, without the Government program, you end up with a net loss of $7.32 an acre and with the Government program, $14.28 per acre on the positive side.

If you can punch the yields up like some areas of the wheat belt in the 40-bushel-per-acre range, there is some profitability in wheat. We raise it because we don't know what else to do with the land, and with the cattle we can usually make it work.

EQUIPMENT AND MACHINERY PROBLEMS DUE TO PROFITABILITY

During the 1980's, those that entered into it without much debt load have been going backward. I know a couple of substantial, well-established operators that have made the statement to me in the last 6 months that, "With the 1985 farm bill, yes, we have some profitability back into it, but we still have the rust belt going on because there's not enough profitability to replace the equipment and machinery that we're using."

I know several tractors that have 8,000 to 10,000 hours on them. We normally put anywhere from 1,000 to 1,500 hours per year per tractor, and if you take that at 50 miles an hour, that's a half a million miles at 10,000 hours. There is very little replacement that has been going on in our area. When it got down to where it was just an absolute necessity, it's replaced. This has a spin-off effect in the entire American economy. The steel mills don't work, the tractor factories don't work, and the pickups and all the auxiliary equipment that goes with it.

ADDRESSING THE WHEAT PRODUCTION COST DECREASING

In addressing the wheat production cost decreasing in the last few years, that is about the same time that the banker would tell you, "I know you need 100, but you're going to get by on 50." So that was pretty common, the best I can tell, across the entire U.S.A. In fact, you know that Oklahoma has had a large number of banks that went under due to agriculture and oil problems. One of those guys saved a pretty nice filling station when he lost his bank. It took him 2 years to go broke at that because he wouldn't sell anybody over half a tank. It's a problem that goes on and on.

DEMISE OF EQUIPMENT DEALERS AND FARMERS

In 1980 we had four equipment dealers in Altus, and it's a good agricultural area. We raise quite a bit of irrigated cotton around there. Today we have one.

Senator PRYOR. One dealer? And there were four equipment dealers 10 years ago?

Mr. FELTY. I understand we have a new one coming in, but I haven't witnessed that yet. So we will wait and see on that.

Senator PRYOR. Have you been in this area most of your life? Is this the native part of the State for you?

Mr. FELTY. Yes. I've been there 47 years.

Senator PRYOR. Forty-seven years.

Mr. FELTY. It's always been home.

Senator PRYOR. Do you have more or less or fewer farmers today than you had in 1980?

Mr. FELTY. We have fewer farmers, and I foresee, it's not as rapid a decline but there will be some more that go out.

Senator PRYOR. Do you see any young people in this area going into agriculture?

Mr. FELTY. A few. Usually those that are going into it and have a reasonable chance of making it are people that their dads are reaching retirement age and have enough volume that they can go into it. I have witnessed several go in and fail. There just wasn't enough income there to support two families.

Senator PRYOR. One of your Senators, Senator Boren of Oklahoma, is a very distinguished member of the Agriculture Committee, and he, like Senator Baucus and myself, were struggling with the 1990 farm bill. Do you have any advice to give us?

Mr. FELTY. Well, I sympathize with you in your problem. [Laughter.]

Senator PRYOR. I sympathize with you in yours.

Mr. FELTY. I have sent quite a bit of advice already. I don't know whether it will all be heeded or not. It would probably be dangerous if it was. [Laughter.]

TARGETING OF PRICES

We mentioned targeting of prices a while ago (previous testimony). Well, on a 1,500-acre wheat farm in southwest Oklahoma, and that large volume of crop that we were talking about, it takes about 1,500 acres just to make a fair living. And then you have to run the cattle on it. Well, that would run about 500 steers. At this year's prices, 500 pound steers, about $1 a pound, that's $500 per head.

So just the fact that you bought the steers and sold them, whether you made any profit you could even lose money on them actually by the time you put the interest and everything else in, but there's $250,000 worth of gross income without—you know, it's zero or actually it would be less than zero because that's a straight pass-through. It doesn't count any processing, any trucking, any pasturage, vet bills, interest, all of those things.

So, targeting, it scares me pretty bad, and I think it would be punitive on the production where the big base of the production comes from.

You know, Senator, in the 1950's, when I was growing up, the statement was, "The world population is increasing at this level, and we are the only Nation that can feed them." I heard the same thing in the early 1960's when I was in college. We tried it in the 1970's. The only problem was, not anyone figured out who was going to pay for it, and we can't afford to be the residual supplier for the world.

I probably could tell quite a bit more, but I will terminate at this point.

Senator PRYOR. Well, we want to thank you very much, Wiley, for coming and expressing some of the concerns of the wheat farmer of our country.

What does a wheat farmer, when the housewife or someone goes into the local food store and buy a loaf of bread, say, for $1 or so, what does the wheat farmer get out of that?

Mr. FELTY. If memory serves, a little less than 2 cents.

Senator PRYOR. About 2 cents. That's the figure I have seen, and that is the purpose, I think, or one of the purposes of today's meeting is to sort of educate people to that fact. And we have some other facts and figures we are going to present for the record that will help to support that finding.[24]

Wiley, we really appreciate your coming today.

Mr. FELTY. The further you get from the patch the more valuable it becomes.

Senator PRYOR. Yes. Thank you very much. We appreciate this very much.

Mr. FELTY. Thank you, Senator.

Senator PRYOR. Thank you, sir.

Our next witness is Billy Joe Miles. He is a fertilizer retailer from Owensboro, Kentucky. I believe that if I am correct, Owensboro, Kentucky, is probably the hometown of Wendell Ford, the distinguished Senator from Kentucky.

Is this correct, Owensboro?

Mr. MILES. That's right. He is from Owensboro.

Senator PRYOR. Thank you. Senator McConnell is a member of this committee. I am sorry he could not be with us today. But I know Senator Ford will be glad one of his fellow hometown citizens is here. We look forward to your statement, Billy Joe.

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[24] See pp. 537–548 for the facts and figures referred to by Senator Pryor.

STATEMENT OF BILLY JOE MILES, FERTILIZER RETAILER, OWENSBORO, KY

Mr. **Miles**. Thank you, Senator.

INTRODUCTION

I am sure everyone is thinking about lunch right now, those that aren't asleep. Maybe we can put you all to sleep and some of us can have two plates. [Laughter.]

I kind of wear three hats today. I wear first the hat of a farmer. I farm a large acreage there. And I run a farm supply store and have 19 farm supply stores. And then I have a chemical and seed distribution company that I distribute seed and chemicals in Kentucky, southern Indiana, southern Illinois, some in Tennessee.

So basically I really have my roots in farming and have one of the larger farming operations. I can sympathize with what everyone said today.

PRODUCTION COSTS FROM THE FARM SUPPLY SIDE

I would like to bring up the production costs and talk a little bit about from the farm supply side of this thing. Really, whatever happens to me as a fertilizer retailer dealer or distributor in turn happens to the farmer.

First of all, in the retail fertilizer business, my big nightmare is insurance. My insurance costs have gone up about 600 percent over the last 15 years.

And the sad thing about that, not only I but almost every fertilizer dealer in the United States or chemical dealer, doesn't have—and I guess I shouldn't say that, because I do have some—we really don't have officially any environmental protection insurance if we have a chemical spill or a nitrate spill that would get in the water. The only way you can possibly insure is just take a lot of life insurance and be ready to jump off the bridge if something bad happens. [Laughter.]

THE ENVIRONMENTAL ISSUE

The other thing is that the environmental issue is something that really haunts me. The big part of my overhead in my operation 3 years ago was 4 percent. Today it's 7 percent of my operation, 3 percent but almost doubling. And that is caused by the paperwork and overhead that I do in this. All the community right-to-know and all of these things are essential. They're good things. They're things that should be done to protect the environment, protect the consumer, and protect the people.

But as you look at this, it really gets complicated. And it's very complicated and it's a lot like the wetlands on my farm: If a farmer comes in or we take out chemicals and it's mixed in the fertilizer, we have to give a materials data sheet to go with that. And with my insurance and with the trucking industry as it is, they have to be put in order according to the danger of those things. And you can imagine how complicated that gets as you make delivery.

THE COSTS OF FARMING

Another thing that was referred to here today is the cost. Labor costs have gone up dramatically for two or three reasons, but the main reason, agriculture hasn't been a glamour industry, so we haven't had a lot of people go into agriculture lately. And to operate the equipment, to do the things that need to be done within the environmental problems we have, it takes someone really with a B.S. degree in agriculture and, hopefully, a little bit of biology and other things to be able to work in a fertilizer store.

Equipment costs, just like on the farm, are horrendous. I think that is probably the biggest increase I have had.

Senator PRYOR. Now, what cost is that, Billy?

Mr. MILES. Equipment costs.

Senator PRYOR. Equipment costs.

Mr. MILES. Spreader trucks, fertilizer trucks, when I went in business you could buy a Chevrolet truck and a fertilizer bed, $6,000 for the truck, $4,000 for the bed. Good truck for $10,000. This year I have added four flotation equipments in excess of $100,000 apiece. So equipment costs are really going up.

The same way on the farm, when I got out of college I bought a six-row planter, $1,200, $200 a row. Last year I bought a 16-row planter, $70,000, or about $4,000 a row.

So the equipment costs continue to go up, and as we supply the farmer with fertilizer, they just continue to go on and on.

There has been a little bit of talk about the charge in deep-freeze production costs there, and you have asked several people about that. About that time, we had potash prices, we had phosphate prices, we had overproduction of world fertilizer. Since then we have had some tariffs. The tariffs on Russian urea. We have also had some duties and some voluntary things that have happened. About 5 percent of our fertilizer was coming from Carlsbad, about 95 percent from Canada, and there was a lawsuit filed to raise that, and they have voluntarily raised the price.

Another big increase is freight. In the past, I could get fertilizer out of Florida by rail, $12 a ton. Now it's $50 a ton by rail.

Another big cost that I have had is I have had a lot of the chemicals that I used to sell my farmers that were not re-registered, will not be able, because of the cost to be registered. And we are using chemicals today that are a lot more expensive that will replace some of these others. The chemical companies absolutely can't afford the cost of re-registration of a lot of the chemicals.

OUR BAD DEBTS ARE AT RECORD LOWS FOR FARMS

You had a banker on a while ago, and I think one of the things that as a farm supply dealer I am really a banker and have been involved in that some. Our bad debts are at record lows for farms, and I think that is because of the 1985 farm bill.

A 1990 FARM BILL AS A PROTECTION

I really shiver in fear of what would happen to me as a farm supply dealer and as a farmer without a 1990 farm bill as a protection so that when that fellow comes in to buy his fertilizer or his chemicals I at least have an idea of what his income is going to be that year so that I can face him, give him credit, put the money on the books, and know.

CROP INSURANCE

The other thing I am a little concerned with is crop insurance. About 25 percent of the credit that I have are customers, I have about 12,000 customers in all, some small, some big, but a lot of those, about 25 percent, is financed internally by me. And without the farm bill and crop insurance, I absolutely would have to turn those people away.

CONCLUSION

I would, in closing, like to say the one thing, the best friend that the consumer in this country has is a good farm bill to ensure a cheap, good supply of food for him in the next 5 years.

I appreciate being here. This is a wonderful thing you are doing. Thank you.

Senator **Pryor**. Billy, I think you have summed up what this hearing is about much better than I did when you said that the best friend the American consumer has is a farm bill. And I think you would agree with me that it is also the farmer, because that's the one that farm bill is basically written to protect and to encourage. And it's a hard thing, as you know, to craft a farm bill that is balanced and tries to serve the purpose of not being too expensive for the taxpayer but yet allowing the U.S. consumer to spend less on food than consumers in any other country. And I will put that chart in the record at the end of our hearing. Also, a chart, a table indicating that food costs worldwide, 1989, once again the Americans come out far ahead of the pack.

Also, there is a farm income support table which indicates here that even though the farm programs are, yes, expensive, that the average farmer out there in this country is a long way from getting rich or ripping off the system.

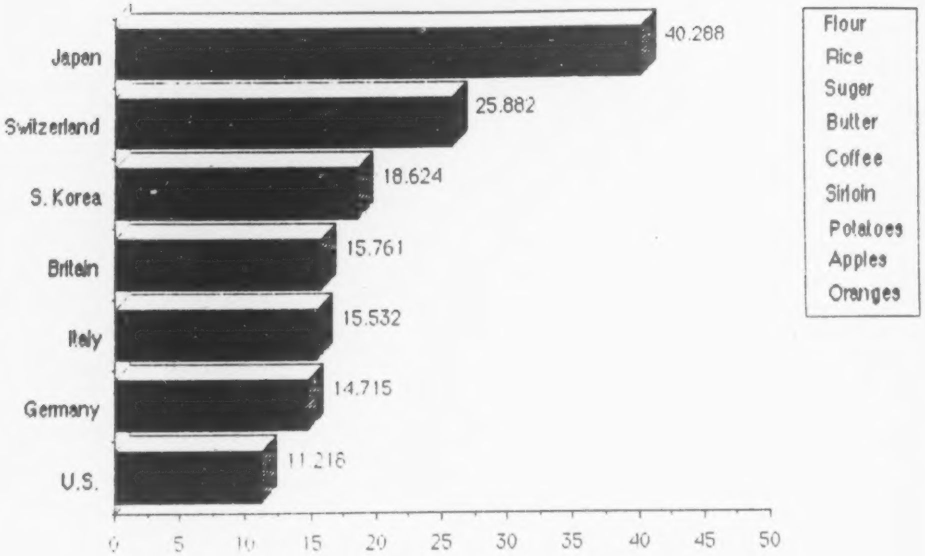
[The material referred to by Senator Pryor follows:]

U.S. Consumers Spend Less on Food than Consumers in Any Other Country

Country	% Income/Food
Sudan	62.9
Sierra Leone	57.9
India	53.3
Philippines	51.5
China	47.8
Iran	45.0
Sri Lanka	43.8
Venezuela	42.0
Honduras	41.3
Jamaica	38.6
Jordan	37.2
Korea	36.3
Thailand	35.7
Greece	34.6
Portugal	32.9
Mexico	31.9
Ecuador	31.3
Colombia	31.0
Cyprus	30.2
Malta	28.3
USSR	28.0
South Africa	27.6
Israel	26.8
Spain	26.2
Fiji	25.2
Ireland	24.8
Puerto Rico	23.4
Italy	21.5
Singapore	21.1
Switzerland	20.2
Iceland	19.5
Norway	18.9
Finland	18.8
Japan	18.8
Sweden	17.9
Belgium	17.7
Austria	17.5
France	16.8
West Germany	16.8
Hong Kong	16.5
Denmark	16.4
Australia	15.5
Luxembourg	15.5
Netherlands	14.4
United Kingdom	13.7
Canada	11.5
United States	10.4

Source: United Nations System of National Accounts as reported by USDA/ERS in "National Food Review," December 1989

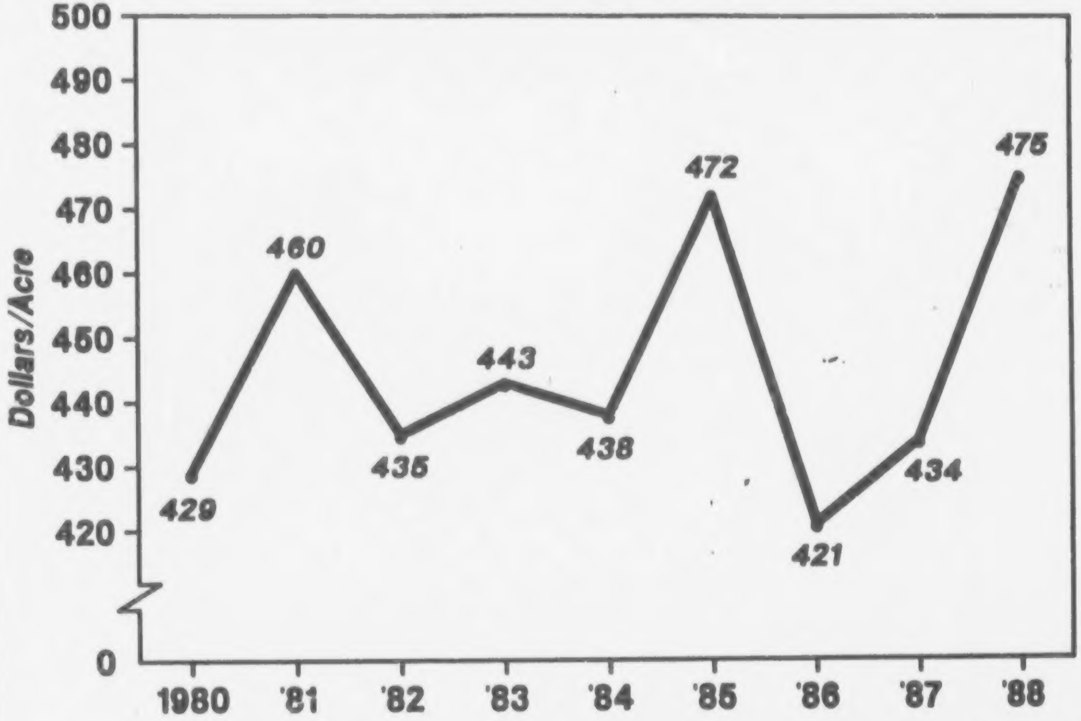
Food Costs Worldwide 1989



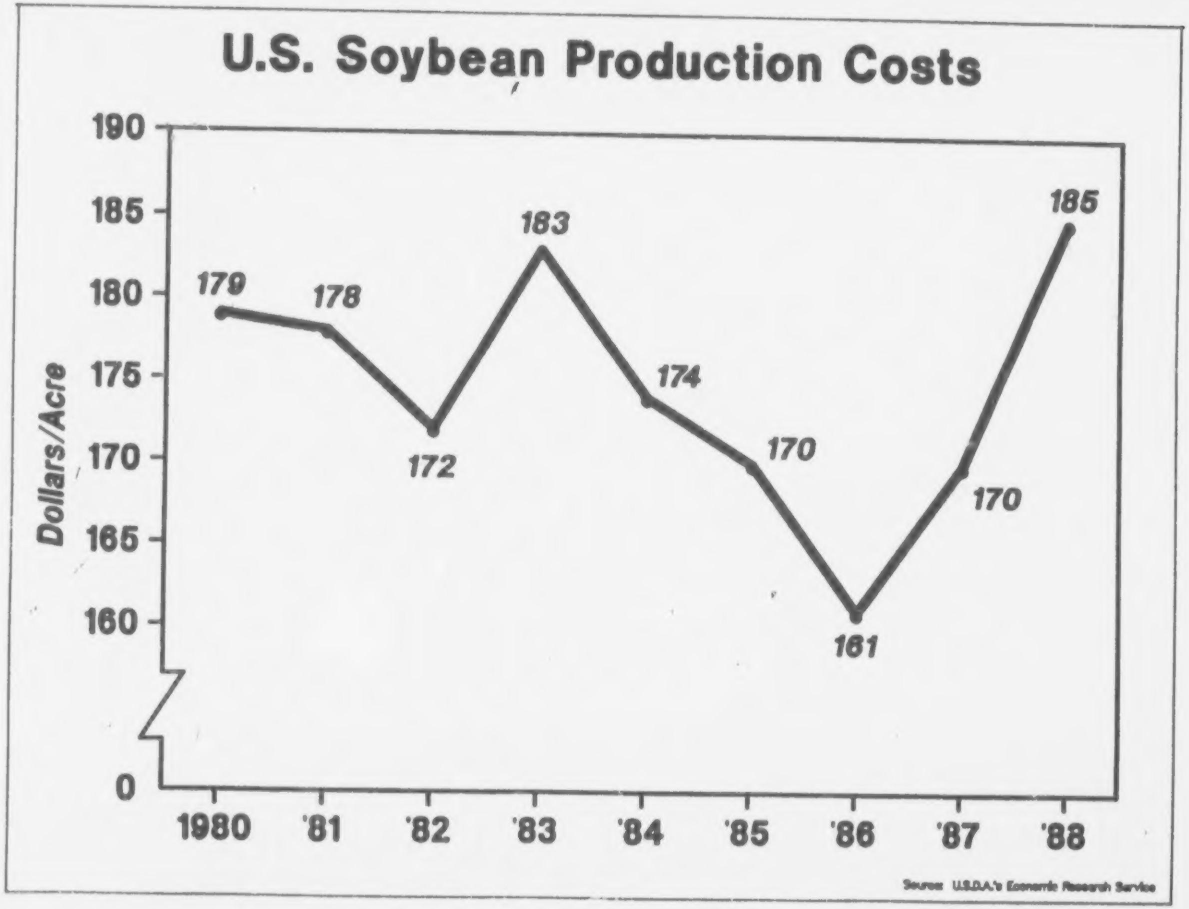
Aggregate Total (Dollars per pound) of Selected Food Items

Source: Foreign Agricultural Service of USDA

U.S. Rice Production Costs

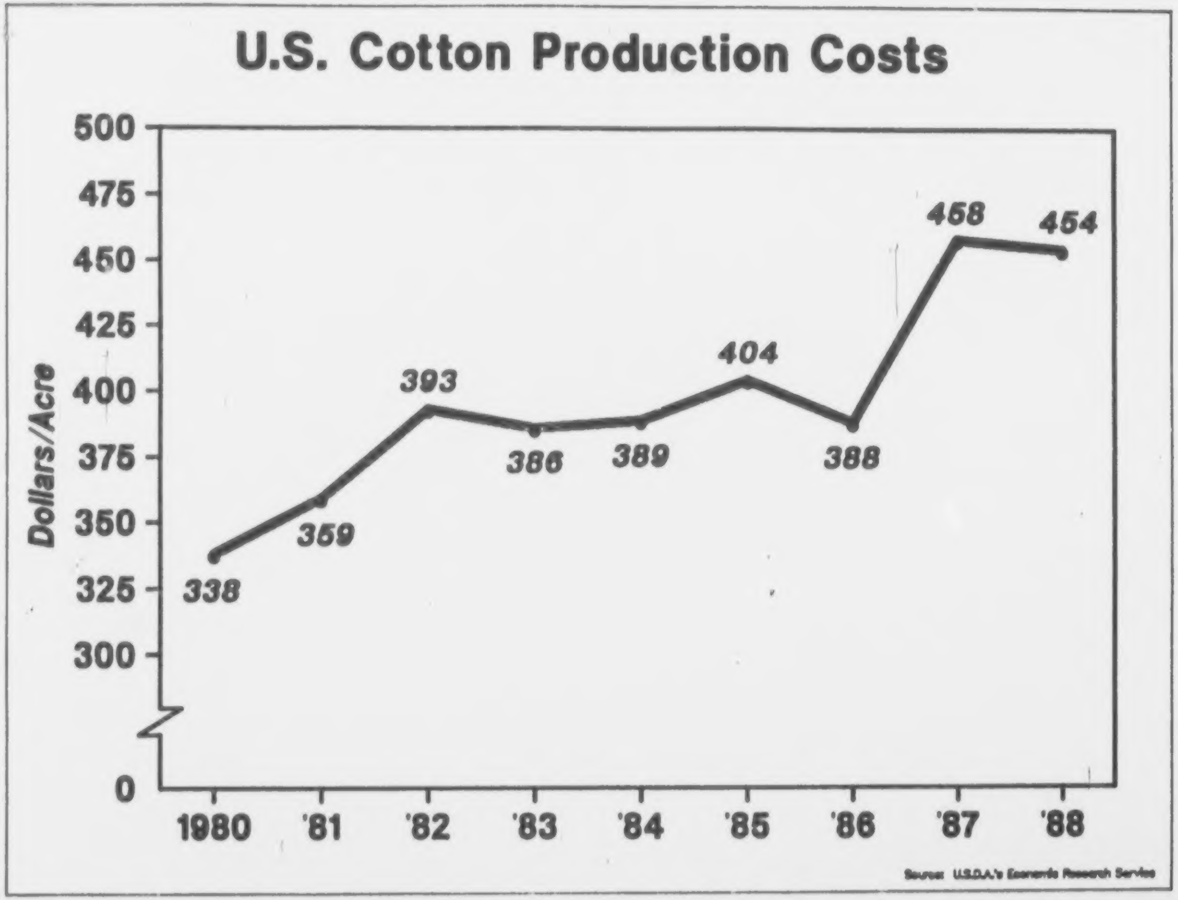


Source: U.S.D.A.'s Economic Research Service



U.S. Soybean Production Costs

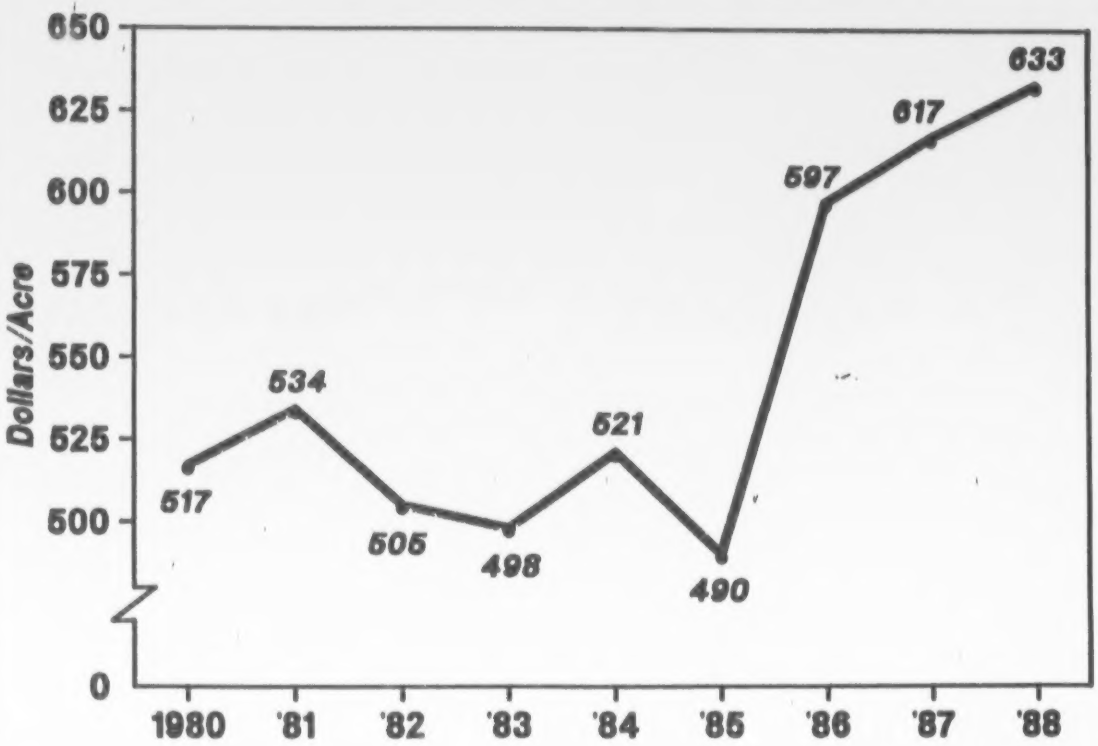
Source: U.S.D.A.'s Economic Research Service



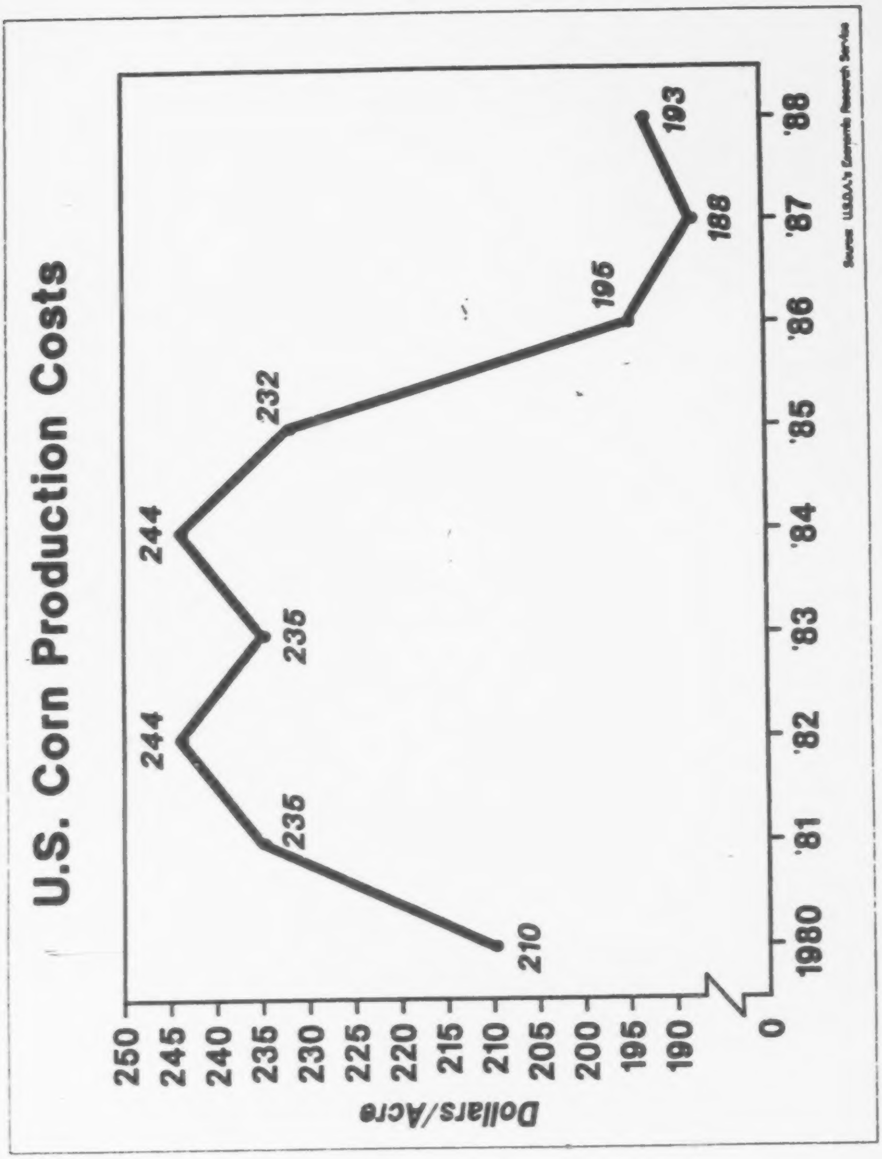
U.S. Cotton Production Costs

Source: U.S.D.A.'s Economic Research Service

U.S. Peanut Production Costs



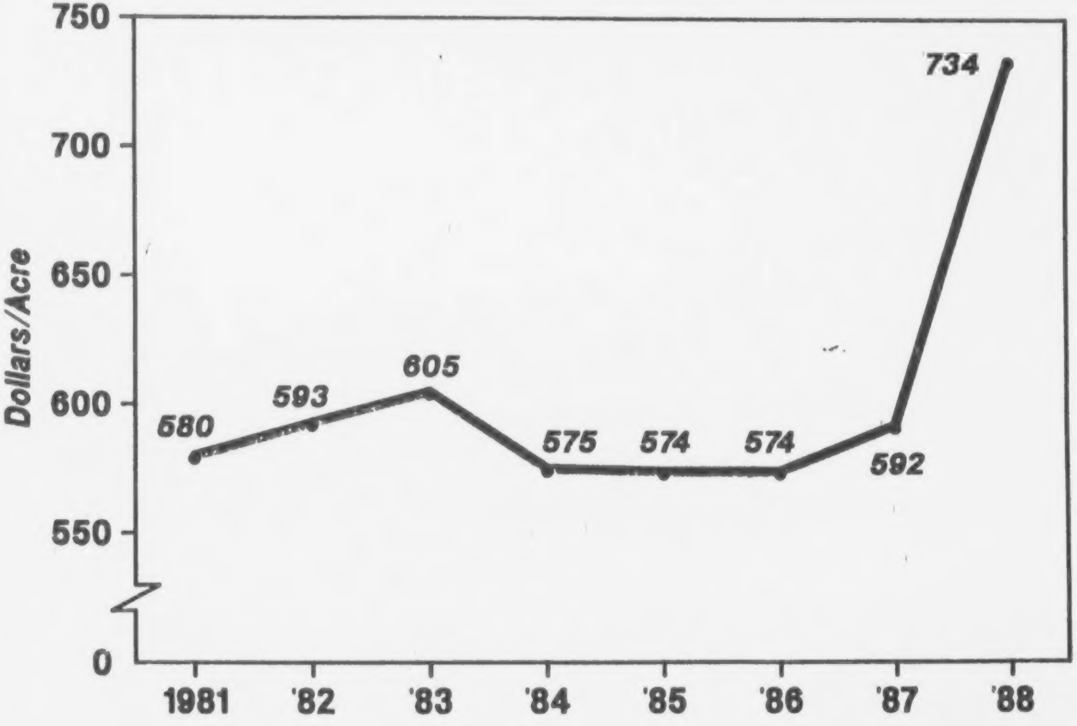
Source: U.S.D.A.'s Economic Research Service



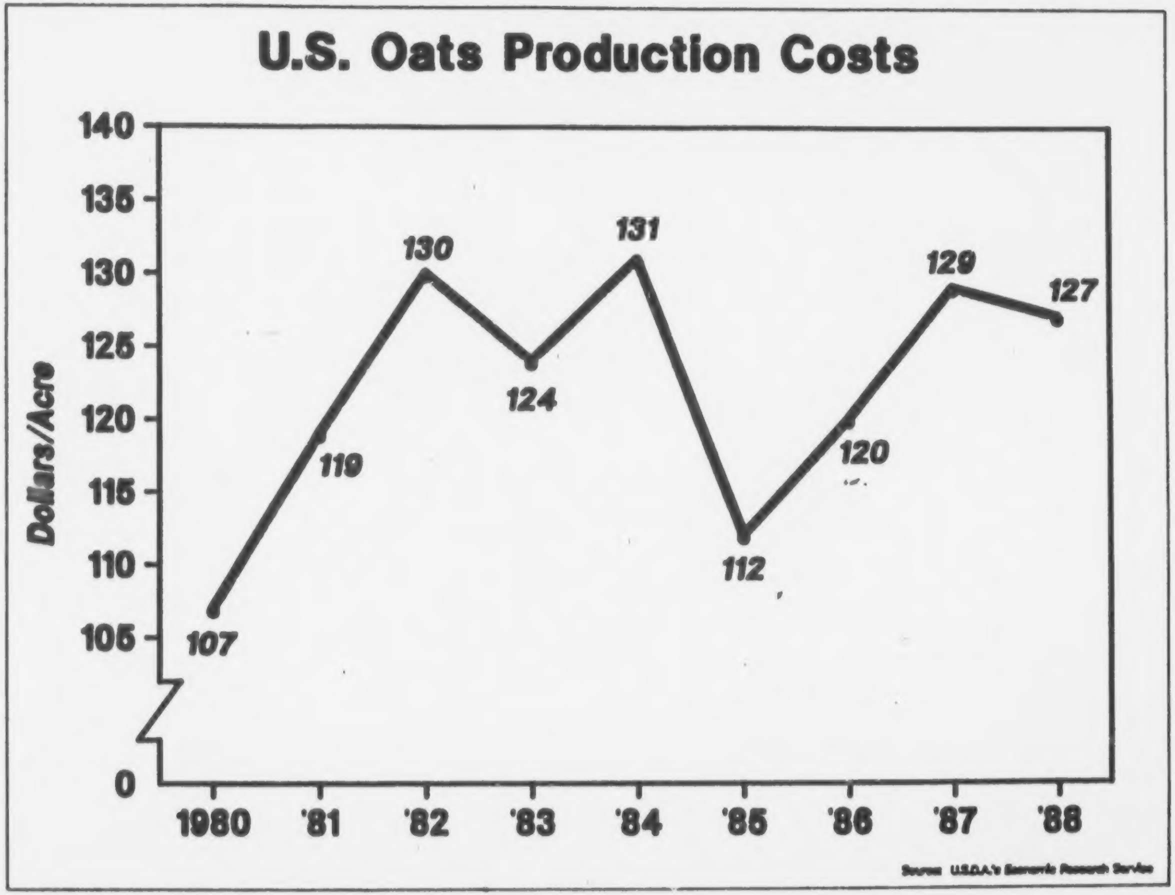
U.S. Corn Production Costs

Source: U.S.D.A.'s Economic Research Service

U.S. Sugar–Beet Production Costs

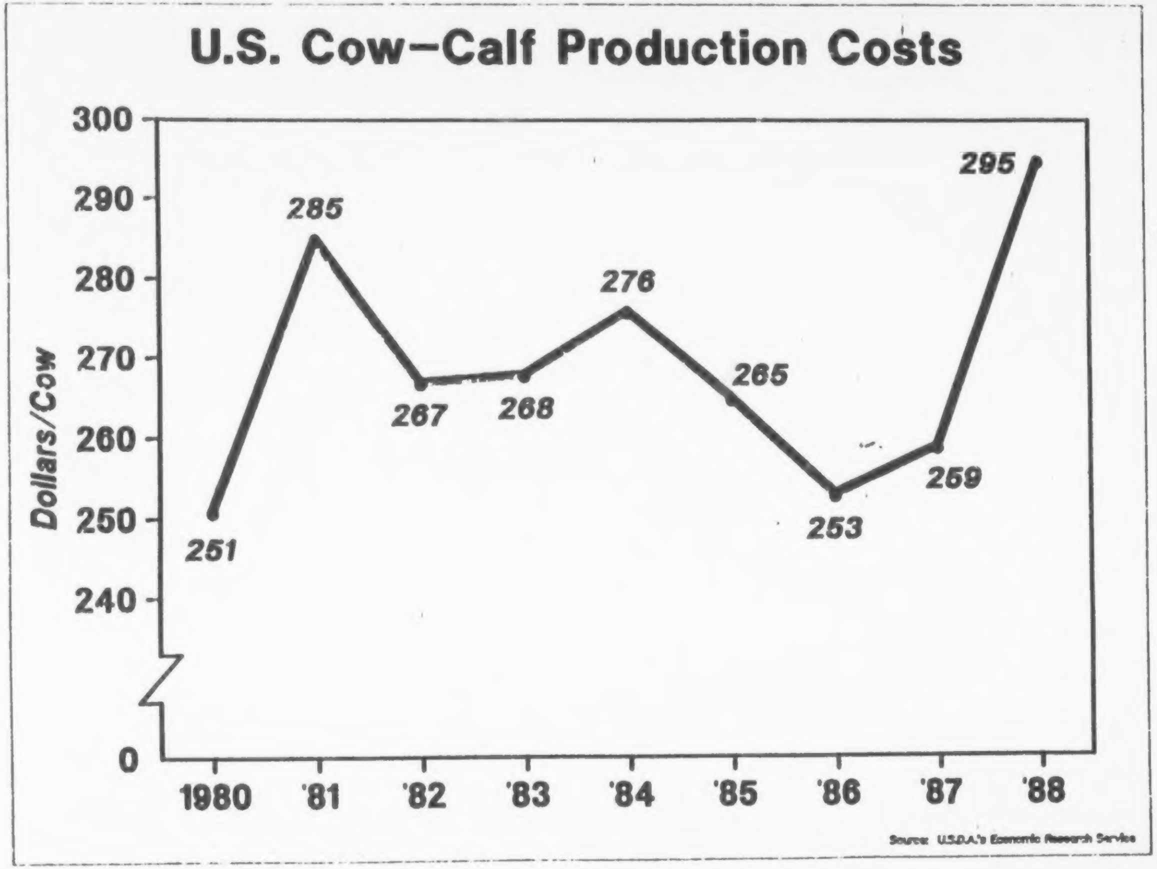


Source: U.S.D.A.'s Economic Research Service



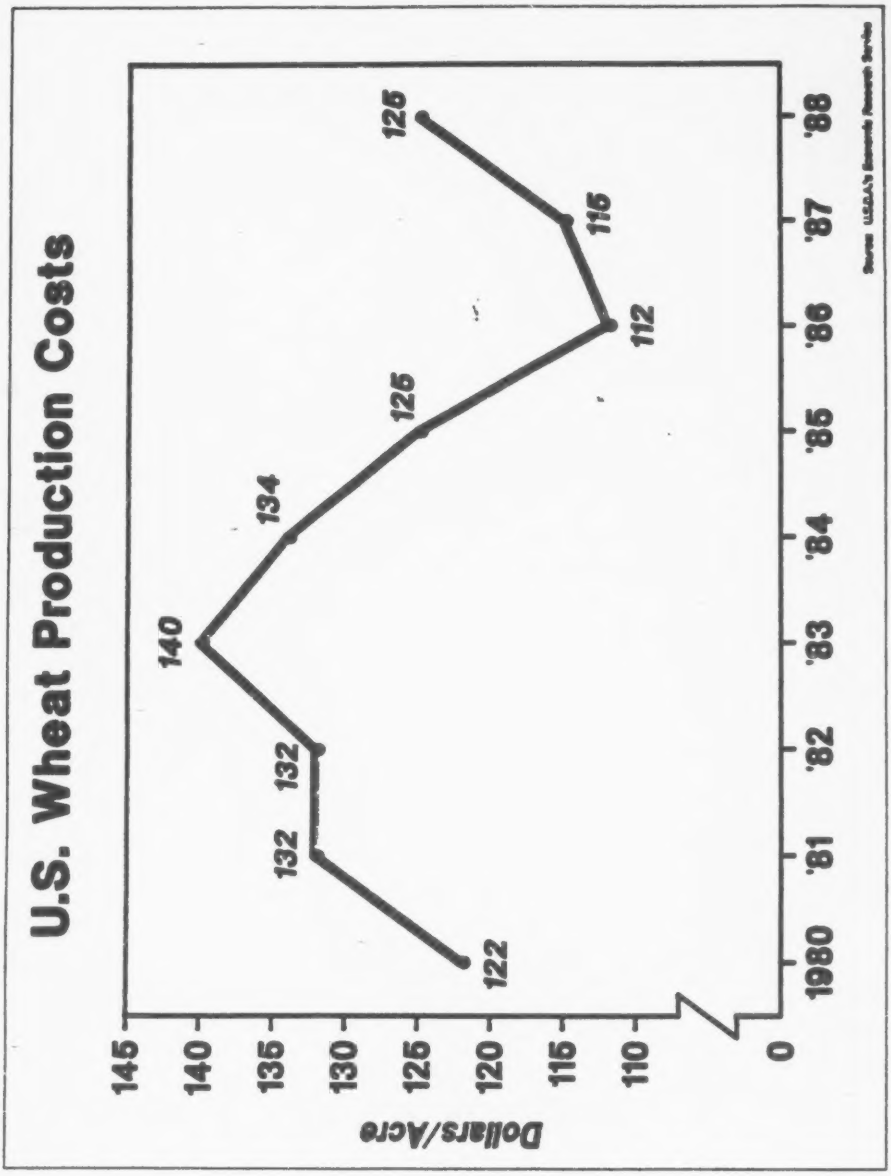
U.S. Oats Production Costs

Source: U.S.D.A.'s Economic Research Service



U.S. Cow–Calf Production Costs

Source: U.S.D.A.'s Economic Research Service

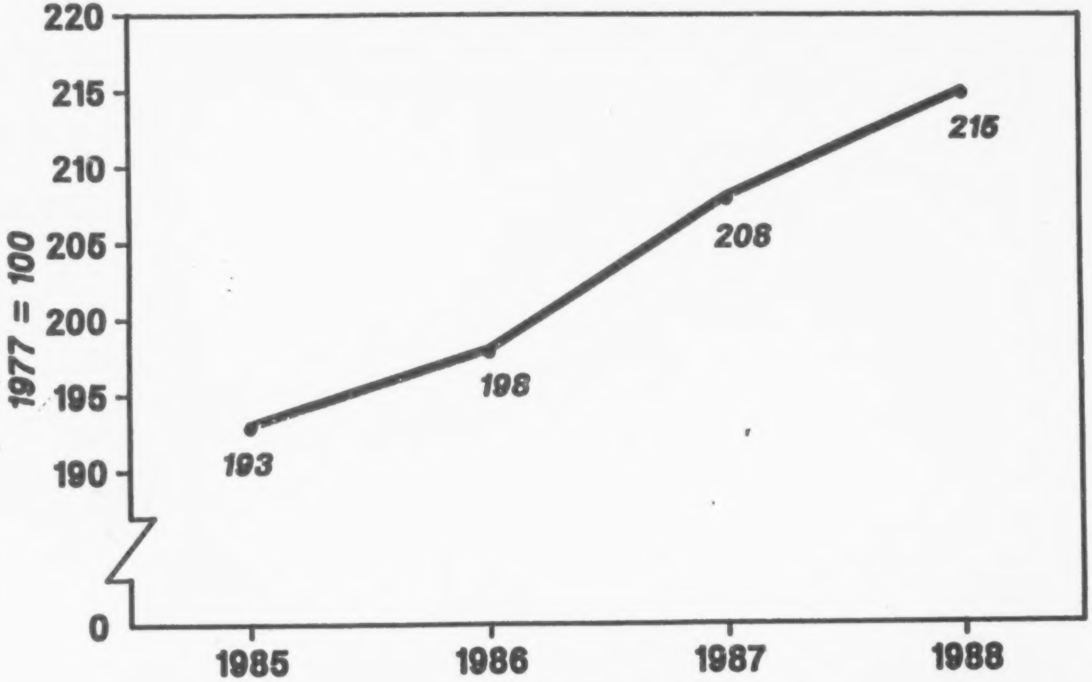


U.S. Wheat Production Costs

Source: USDA's Economic Research Service

Cost of Farm Equipment (autos & trucks)

1977 = 100 (inflation adjusted)



Source: U.S.D.A.'s Economic Research Service

Senator **Pryor**. So we are going to try to basically set this record straight as the debate ultimately continues in the Agriculture Committee, as our bill goes to the Senate floor and to the House floor and ultimately to a conference.

We have an education job, and one of those real challenges we have is to help educate some of our own colleagues here in the U.S. Senate and in the House about some of the tremendous costs of production problems the American farmer has had. And we are trying to do that now, and that again is one of the purposes of this hearing.

Once again it is our invitation to invite all the participants this morning and all the audience to a little lunch.

You are going to also get a little luncheon tab at your table as to how much this lunch costs—by the way, you don't have to pay it; none of you do—how much this same lunch would have cost 10 years ago, and how much the increase has been, how much the net income to the American farmer has been in those 10 years from this lunch that we are serving today.

But I want to thank all the witnesses. Some of you came from a long way, and it is at this point 12 o'clock. I think it would be appropriate now to adjourn the meeting, have our lunch. And if any of the members of the press want to visit with our witnesses, certainly they are invited to do so.

Thank you. The meeting is adjourned.

[Whereupon, at 12:01 p.m., the subcommittee adjourned, subject to the call of the Chair.]

[Material submitted for inclusion in the record follows:]

APPENDIX

PREPARED STATEMENT OF HELEN WALLER, AGRICULTURE POLICY COMMITTEE CHAIR, NATIONAL FAMILY FARM COALITION, WASHINGTON, DC

Thank you, Chairman Pryor for soliciting the input of concerned family farmers in your hearing on the issues associated with costs of production on the farm. This is truly the point from which all considerations of the 1990 farm bill should start because that is where the greatest shortfalls of the 1985 farm bill and all farm policy within recent memory begin.

I should begin by saying that my name is Helen Waller. My husband, Gordy and I raise wheat, barley and have a livestock operation in eastern Montana. I am the Chair of the Agriculture Policy Committee of the National Family Farm Coalition (NFFC). The NFFC is comprised of 40 farm and rural organizations in 35 States who are committed to preserving and strengthening the family farm system of agriculture.

The goal of the 1990 farm bill should be declared up front to be: **"The preservation of family farming as the main source of affordable, stable supplies of food and fiber produced by environmentally sound practices for the sustenance of the American people and to fulfill world needs as well."**

With that goal in mind we must examine what is essential to enable producers of food and fiber to maintain the means of production. What is their direct cost to provide the crops for the consumers and what is the real investment that is required to guarantee a long term productive resource base both in human and renewable resource terms? Are we providing an agriculture policy which will address the needs of farmers, consumers and future generations? The answer is all too clearly, "No!", if one looks at the effects of the 1985 farm bill for lessons in developing a 1990 farm bill.

In my home county, McCone County, Montana the 1989 prices for Spring wheat do not provide income necessary to cover costs of production even when management and labor are excluded. North Dakota State University reported in February of 1990 that if real costs of equipment, conservation practices, land taxes, and debt are considered that a farmer in my area can, on an average, expect to lose $1.16 an acre on a 1,000 acre farm model. Due to fallow conditions and a 24 bushel an acre 6 year average yield that is not an unusual model.

No farmer, particularly a reentering or beginning farmer, can hope to engage in realistic long term, responsible farm management, conservation practices, machinery replacement and land related expenses on the basis of today's crop valuations. We have an average age of 58 for farmers in this country because, unless you have full equity in your farm, it is not likely that you have fared well enough in the last 5 years to survive to grow another day. The bad news is also that once you have left farming the chances of your returning to farm ownership are almost nil.

At a time that discussions in Washington seem to revolve around minor adjustments to the 1985 Farm Security Act, let me relate how I see the 1985 farm bill is "working" in relation to producers and their main street suppliers, and for the grain traders and processors.

How is it "working" for the farmer? Since the 1985 farm bill was passed, according to the American Banker's Association, over 400,000 farm families have left the land. For every five farmers out of business, one main street business closes. In rural communities, health care and quality of education are deteriorating because of the depression.

Our purchasing power has been wiped out. As an example, in 1973 it took the gross sales of 15 calves to buy a pick-up. Today it takes 45 calves to buy a similar vehicle. In 1973, 4,250 bushels of wheat would buy a 125 horsepower tractor. Today, for the same size tractor, it takes 13,577.

The systematic depression of grain prices through "Secretarial discretion" to "market clearing" prices has been the main thrust of the 1985 Food Security Act. The deficiency payment method of subsidies, which pays the difference between depressed market prices and target prices which do not reflect true costs of production, has led to budget busting agriculture expenditures. It has not, however, provided security to America's family farmers and other taxpayers. It has maintained much of our foreign market share but even that has come at a cost of $2 for every $1 increase in export market value, leading St. Louis Federal Reserve economists Cletis Coughlin and Kenneth Carraro to observe, "Destroying the government owned stocks . . . would be a more cost-effective form of surplus removal than the EEP . . .".

Meanwhile, billions of taxpayer dollars have gone into the farm program allowing the grain handlers and processors to buy commodities at fire sale prices, reaping record profits while farmers continue to go broke!

There is little correlation between prices received by farmers and food prices at the retail level. For example, when the return to the farmer on the amount of wheat in a box of cereal fell by 33 percent, the consumer price for that same box of cereal rose 84 percent. The processors bought the grain at a subsidized low price, but failed to pass the savings on to consumers.

Where did the money go and who actually got the subsidy? Agribusinesses have profited mightily from the 1985 farm bill. ConAgra, the number one U.S. wheat miller, reported a 43 percent total return to investors over the past decade.

Cargill controls one-fourth of the world's grain trade, and in 1986 reported a 66 percent increase in profits. Their subsidiary Caprock industries, is the third largest cattle feeder. Continental Grain is the fourth largest cattle feeder and the third in grain trading.

Even as we meet today, the Attorneys General of five States, including my own, have launched a Justice Department complaint asking that antitrust action be taken to prevent any further concentration in the meat industry until a full investigation can be completed.

These giant companies rapid control of the food supply, not only in the United States but globally, should be of grave concern to Congress as the new farm bill is written. The artificially low market price of feed grain, as achieved in the 1985 Food Security Act, has been the major incentive for three huge corporations, Cargill, ConAgra and Iowa Beef Processors (IBP) to gobble up nearly 80 percent of the beef processing industry.

Their control of feedlots, which together with Continental Grain, represents an annual capacity to feed nearly 1.5 million head, only underscores our concern that low feed grain prices have created a noncompetitive position for small family owned feedlots in the Midwest who raise their own feed. It has effectively driven them out of business. Therefore, competition in the Midwest to feed out Montana calves is virtually nonexistent. Many Montana ranchers who a few years ago ran yearlings on grass, have converted to cow/calf operations because under a cheap grain policy, Montana grass is no longer competitive. Unquestionably, the price of feed grains sets the value of my grass.

Any consideration of the cost of production of crops and livestock must recognize that revenue for one agricultural producer may be at a cost to another. For example, higher feed grain costs increasing the cost of production for poultry, hog and cattle producers. In the long run, it will also increase the price producers get for their livestock. Livestock prices lag behind but follow feed grain prices, for a variety of reasons summed up in the old addage, "cheap corn means cheap hogs." Higher feed grain prices will also make my grass and other noncrop forage more valuable.

Traditionally, U.S. farm policy has not tried to reconcile the conflicts arising from the interdependence of the different sectors of agriculture. As a result, farm bill debates have often pitted grain producers against livestock producers, to the ultimate satisfaction of neither. Yet, clearly, the future of family farming is at the mercy of Congress.

I believe the proper role of government is to assure that giant corporations do not exert unfair power in the marketplace. If Congress is serious about preserving the family farm system of agriculture in this country, then they MUST establish a price support level which is relative to production costs and which will affect an upward movement of prices in the marketplace.

Without a doubt, current farm policy is destroying the economic viability of family farmers and rural communities throughout America, while multinational grain corporations are making off like bandits, with ever-increasing control of the food supply from my farm gate to your dinner plate. How do we decentralize that control?

Agriculture policies which would reverse that trend are the Heart of the proposed Family Farm Act, a copy of which I will attach for submission into the record as well. The Family Farm Act would:

1. Reestablish cost of production (including a reasonable profit and return on investment) as the basis for grain program support programs. Loan rate increases can show budget savings and return farmer income from the marketplace rather than from a government check. Target prices can reflect true COP.

2. Farmers would participate in effective production management through a bushel based marketing quota rather than the current ineffective acreage based programs which encourage unsound chemical use and fertilizer to boost farm income short term while neglecting the environment long term. Bushel option would allow full use of the farm to achieve production goals with sustainable farm methods.

3. A Farmer Commodity Reserve of onfarm and commercially stored grain would be established. This would allow farmers to store overproduction grain in a short supply year and to cushion the risk for farmers who enter sustainable agriculture programs. Such legislation could eliminate the need for disaster payments and cut costs of any Federal Crop Insurance Program.

4. Livestock producers with annual gross sales below $1.5 million would be eligible to buy up to $50,000 worth of grain from CCC inventory at a discount. This allows breathing room as farm gate prices for meat catch up with higher grain prices which more truly reflect costs.

We must reverse the trend toward greater concentration in the food industry and maintain a broad based family farm agriculture. Former Supreme Court Justice Louis Brandeis once said, "We can have democracy in this country, or we can have wealth in the hands of a few, but we cannot have both".

It is up to Congress to adopt farm policies which will strengthen the family farm system of agriculture in America. It is the foundation of our democratic society.

Thank you.

[The proposed Family Farm Act 1990, submitted by the National Family Farm Coalition follows:]

National Family Farm Coalition

80 F Street, N.W., Suite 714 Washington, D.C. 20001 (202) 737-2215

FAMILY FARM ACT 1990

COMMODITY TITLE

• PURPOSE

A bill to provide a stable and affordable supply of certain crops, grown under more environmentally sound practices, calling for a referendum of producers on the question of establishing price supports at a level covering the cost of production for crops grown, beginning with the 1991 crop season, and for other purposes.

• **DEFINITIONS** --- to be inserted as the final bill requires

• DETERMINATION OF QUANTITY

The Secretary of Agriculture shall determine the quantity of the national marketing quota for a commodity by estimating the quantity utilized to meet (1) domestic demand, (2) export demand, (3) food assistance requirements, (4) domestic reserve requirements, (5) Farmer Commodity Reserve. This determination would be reviewed by the Senate and House Agriculture Committees annually to ensure oversight and opportunity for public review.

• PLANTING INTENTIONS

A producer would declare by a designated time, to the ASCS office, their planting intentions. A producer may shift up to 20% of their crop base each year, to another program crop without losing crop base.

• MARKETING CERTIFICATE POOL

Pool for base adjustment: After the Secretary determines the quantity of a commodity needed, for a period of five years, a pool of marketing certificates representing a percentage (for example 1/2%) of the total marketing certificates available, and in the event that an amount of a commodity established as a National Marketing Quota is greater than 100% of the base acres for that commodity, the quantity exceeding 100% would be allocated to the County ASCS Committees for distribution to: (1) correct base to cropland ratio inequities, (2) help beginning and re-entry farmers, and (3) arrest the decline of minority landownership.

• CERTIFICATION

After planting, a producer must certify, within 1% tolerance of planting intentions.

* MARKETING CERTIFICATES ISSUED

Marketing certificates would be issued to producers, determined by multiplying a farm's base acres, times established yield, times marketing certificate factor assigned to that farm size. The greater the farm's production, the smaller the percentage of marketing certificates issued.

Marketing certificates percentages shall be based on the following formula:

	CORN	BARLEY	WHEAT	SOYBEANS		Marketing Certificate Factor
Up to	10,200 BU	20,400 BU	9,800 BU	4,800 BU	=	100%
The next	5,100 BU	10,200 BU	4,900 BU	2,400 BU	=	94%
The next	5,100 BU	10,200 BU	4,900 BU	2,400 BU	=	88%
The next	5,100 BU	10,200 BU	4,900 BU	2,400 BU	=	82%
Balance over	25,500 BU	51,000 BU	24,500 BU	12,000 BU	=	76%

After certification, the Secretary will adjust marketing certificates to meet determined need by increasing or decreasing the number of certificates by an equal percentage among every size producer, on a commodity by commodity basis. Total number and allocation of marketing certificates would be determined on each commodity separately.

Acres on which marketing certificates are based, if not planted to certificate crop must be put to a conserving use.

On-farm use of a program commodity will be deducted from the number of marketing certificates issued.

* LIVESTOCK FEED ASSISTANCE PROGRAM

When livestock market prices are below the parity price support level established for small grains, then livestock producers with annual gross sales below $1,500,000 would be eligible to buy up to $50,000 worth of grain from CCC inventory at a price equal to the parity level at which the livestock is valued or they could receive certificates of equal value.

Guidelines will be written to prevent abuse of program.

* OVER-CERTIFICATE PRODUCTION

If a producer who is in compliance with the program harvests more of a commodity than they have marketing certificates for, the over-certificate production may be:

(1) stored on farm for use in a subsequent year,
(2) donated to the CCC for famine relief, including, but not limited to, government administered relief programs,
(3) sold to the CCC for U.S. government food assistance or famine relief programs at not more than 50% of the loan rate, or
(4) sold to CCC for Farmer Commodity Reserve.

* PLANTING OF NON-PROGRAM CROPS

The Secretary may limit the acres of non-program crops if the Secretary determines that it is necessary (1) to maintain farm or ranch income; or (2) to minimize farming practices that degrade the environment.

* PRICE SUPPORT

Price supports on program crops shall be set at 75% of parity as established by USDA, with a 3% per year increase, up to 90% parity.

* SUSTAINABLE AGRICULTURE

A producer may participate in the low input sustainable agriculture (LISA) program by filing a five year farm plan based on provisions in the Low Input Technical Guide. Producers may appeal out of the LISA program after three years for reasons of undue economic hardship. Once they leave the program, they may not re-enter until the five year period is over. A producer's land may enter the LISA program at a rate of not more than 20% per year, or 200 total acres, whichever is larger. Producers whose entire farms qualify for the sustainable agriculture programs at the time the program goes into effect may enter their entire farm into the program.

Funds shall be appropriated for the Soil Conservation Service and local Soil and Water Conservation Districts for administering and staffing land and water restoration projects. Cost-share programs which will enhance soil fertility and/or water quality protection shall be instituted, including but not limited to planting of legume crops.

Improved farm practices, including crop rotation with seeding of legume crops would not result in the loss of base acres.

National low-chemical farming technical guides describing appropriate production systems would be developed by the USDA in cooperation with farmers and technicians with expertise in the hands-on experience of low-chemical sustainable farming. This guide would provide the criteria and guidelines for compliance in the sustainable agriculture program.

The Secretary shall call for and appoint a panel of experts to develop guidelines establishing criteria for the technical guides which will be developed at the regional or state levels.

This panel of experts, as well as state or regional panels shall be made up of nineteen persons: eleven farmers with demonstrated expertise in sustainable agriculture techniques; five USDA representatives, including ASCS, SCS and Extension Service, all of whom are involved with the low input sustainable agriculture program; and three representatives from non-profit sustainable agriculture research organizations.

No representative on the panel can be employed by or receiving grants from any agricultural input industry or any of these industries' non-profit research subsidiaries, within one year prior to enactment of this legislation.

Technical guides shall be completed within one year of enactment of this bill. The guides will clearly outline acceptable practices and techniques. For example, additional use of chemicals with no-till will not be considered a sustainable farming practice.

Economic risk of reduced income will be insured internally through the Farmer Commodity Reserve. Producers in the sustainable agriculture program will receive a higher percentage of recovery through the FCR.

Non-program crops would be included in the sustainable agriculture program after an affirmative vote in a producer referendum. Participation in the Farmer Commodity Reserve by non-program crop producers would be allowed by assessing a check-off fee.

* PRODUCER COMPLIANCE

Full Compliance -- Farmers would participate in a producer referendum which would require a 51% affirmative vote to require full compliance. If the initial producer referendum passes, the next referendum shall be held in 1996 and each fourth year thereafter. If the initial producer referendum fails, the next referendum shall be held the next year.

* CROSS COMPLIANCE

There shall be cross compliance of crops.

* WORLD FOOD SECURITY AND INTERNATIONAL TRADE

The Secretary of Agriculture is instructed to conduct trade negotiations with the other major exporting nations, to achieve international commodity agreements which would ensure that the U.S. retains its fair global marketshare, as defined by GATT (General Agreement on Tariffs and Trade) and that export prices remain equal to or above average costs of production of the exporting nations.

If the Secretary is unable to negotiate such agreements within such a reasonable period of time, no more than twelve months, then export restitutions, such as bonus bushels or marketing loans, shall be authorized to maintain U.S. marketshare at a level equal to the rolling average of the previous five years.

In order to ensure that the costs of these export restitutions do not rise above current agricultural program spending levels, a Food Reserve Coordinating Agreement would be negotiated through GATT. This agreement would require that all countries share the costs of maintaining global emergency food reserves, and that all exporting countries share the burden of production reductions whenever global reserves exceed agreed upon maximum levels.

These reserves will be effectively and totally isolated from the market.

To insure that such an international food reserve agreement can be effectively implemented, current GATT roles which specifically prohibit export dumping and which specifically permit import and export controls must be clarified to include value-added processed or competitive products and these rules must be uniformly and equitably enforced.

Special and differential treatment within GATT rules for developing countries cannot include the right to ignore normal GATT anti-dumping provisions.

All proposals to GATT which would give international agencies or their appointed experts the power to over-rule local, state, and federal government laws and regulations shall be specifically rejected

Additional provisions must be added to the GATT treaty which can insure that all environmental protection, food safety, and sustainable agriculture programs and incentives are explicitly acknowledged and are in no way, subject to prohibition or restriction by GATT.

* IMPORTS

Agricultural Imports: The Secretary of Agriculture shall, under the authority of Section 22 of the Agricultural Adjustment Act, examine and report to the President with respect to any imported articles that (1) increase the cost of conducting agricultural price support activities; (2) interfere with any program or operation undertaken by the Secretary; (3) reduce the quantity of products processed from agricultural commodities produced in the United States.

Labeling Imported Food: Any agricultural product or processed agricultural product that contains any imported ingredient that accounts for a significant portion of the product's value or volume must be marked to indicate the country of origin of the imported ingredients.

Limitations on Entry.: No agricultural commodity or product may enter the United States if the use of such chemical in the production, processing, or marketing of such article in the United States is prohibited by law. This applies to an agricultural commodity or product; either meat or a meat product, or a live animal used primarily for human food consumption which contains, or on which is present, any residue (or greater level) of any chemical prohibited by law in the U.S.

* FARMER COMMODITY RESERVE

A farmer commodity reserve (FCR) shall be established with available CCC stocks. If additional grain is needed to establish or replenish FCR inventory, the amount of deficiency would be included in the determination of need for the ensuing year. The FCR would also be replenished with over-certificate production, which would be sold into the FCR program at not more than 50% of the loan rate.

Producers who are in compliance with the ASCS commodity program and experience a loss below marketing certificate quota are eligible to draw "like" grain, of equal value from the Farmer Commodity Reserve. If no "like" grain is available within the marketing area, the producer could request equal value in certificates, in lieu of grain. The FCR benefits shall be targeted so that the larger the value of loss, the smaller the percentage of recovery.

Producers could draw from on-farm stored stocks, at which time storage payment would cease. Farmers drawing from commercial storage would pay storage for one year only. The value of grain drawn from FCR by a producer, in any one crop year, shall not exceed $50,000 total.

A farming entity with annual sales above $1,500,000 is ineligible to participate in the FCR program.

Storage bins must meet prescribed standards. Preference shall be given to utilize on-farm storage, then to commercial storage with an emphasis on reserves held in disaster prone areas. Rate for storage of FCR grain shall be the same for on-farm or commercial storage.

In the absence of scale tickets for farm stored grain, ASCS shall provide commodity measurement within a tolerance of 5%. Failure to meet a 5% tolerance will result in payment by ASCS to the farmer of triple damages. Farmers will pay no punitive damages due to ASCS miscalculations. A natural grain shrinkage is recognized.

FCR grain shall be isolated from export dumping.

The FCR program shall be administered by the ASCS, with an Independent County Oversight Board of five members, elected by producers to negotiate disputes. Their decision would be appealable to the state court serving that County or to the federal court at the farmer's choice and expense.

Members of the Oversight Board would be paid at the same rate, and from the same source as the County ASCS committee members. The Oversight Board would meet as they deem necessary, but subject to review by the Sec. of Agriculture. Should the Secretary disband the Farmer Commodity Reserve Oversight Board, the Secretary shall provide for further oversight.

Guidelines will be written to prevent abuse of the program.

* CONSERVATION RESERVE PROGRAM

A county-by-county socio-economic impact assessment of CRP shall be developed for those counties who have reached their 25% cap, before allowing expansion of the national CRP acreage goals. This assessment could be done by an entity other than ASCS, but should, at a minimum, assess the environmental costs and benefits, local tax consequences, and impacts on suppliers, main street businesses, schools and other community services.

Requirements shall be developed for haying and grazing on CRP acres, which would deduct from the CRP payment the value of hay and/or grass. In the event of damage to the grass stand, reseeding and maintenance costs would be borne by ASCS.

Any new CRP contracts shall provide sustainable agriculture options available to landowners in preparation for termination of the CRP contracts. Sustainable exiting provisions in new contracts shall be made available, upon request, to landowners with existing CRP contracts.

* EFFECTIVE DATE

This law shall become effective at the beginning of each program year for the 1991 crop season.

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PREPARED STATEMENT OF DR. ARTHUR M. HEAGLER, ASSOCIATE PROFESSOR, DEPARTMENT OF AGRICULTURAL ECONOMICS AND AGRIBUSINESS, LOUISIANA AGRICULTURAL EXPERIMENT STATION, L.S.U. AGRICULTURAL CENTER AND DR. J.A. MUSICK, PROFESSOR AND RESIDENT DIRECTOR, RICE RESEARCH STATION, LOUISIANA AGRICULTURAL EXPERIMENT STATION, L.S.U. AGRICULTURAL CENTER

First, we would like to compliment the U.S. Department of Agriculture, Economic Research Service (USDA, ERS), for their efforts to recognize the economic impact of government programs upon the cost of rice production. This information is presented in USDA, ERS Agricultural Information Bulletin No. 597 dated March, 1990. The estimates of rice production costs as presented in this report represent an improvement in USDA, ERS rice production costs, however, additional improvements need to be made in order to accurately reflect rice production costs in Louisiana. Consequently, substantial opportunities exist for collaboration between ERS and land-grant institutions to arrive at more accurate estimates of production costs.

A major difference continues to exist, primarily in irrigation costs. This difference is largely due to the difference in methodologies. The methodologies as used by USDA, ERS, focuses upon the costs and returns of all factors of production whether operator or landlord supplied. Such methodology precludes the proper allocation of resources that are purchased with a crop share by a tenant operator. Consequently, differences continue to exist between Louisiana Agricultural Experiment Station estimates of rice production costs in Louisiana and those as revised by USDA, ERS in bulletin 597. The difference in rice production costs for these two estimates (LAES and USDA, ERS) can largely be accounted for by the difference in irrigation costs which includes one-fifth of the rice produced and one-fifth of the price deficiency payment. When this difference is inserted in ERS rice cost of production estimates for 1988, the estimates from the two sources are about the same for all practical purposes (see table 1). Irrigation costs to the Louisiana tenant rice farmer amounts to about $98.29 per acre. If $98.29 per acre is added to the USDA, ERS estimates for 1988, in table 1, the results will show a negative return to management and risk of $64.52 per acre. LAES estimates indicate a negative return of $65.11 per acre or about 59 cents per acre difference between the two sources when appropriate water costs are added to USDA, ERS cost of production. Therefore, the difference which exists between USDA, ERS estimates and those of the Louisiana Agricultural Experiment Station largely reflect the difference between an owner-operator and a share rent tenant. Surveys by USDA, ERS indicate that 92 percent of the rice acreage produced in southwest Louisiana is on rented land. Of this amount, 7-10 percent is cash rented and 82 to 83 percent is share rented. With such a large proportion of the rice acreage being produced on rented land, we submit that rice production costs which reflect the tenant situation, more accurately represent the cost of producing rice in southwest Louisiana.

Rice production costs in southwest Louisiana have increased by about 1.5 percent per year since 1985. Overall, rice production costs per acre have increased by 7 to 10 percent since 1985. Increased productivity has reduced per unit cost about 8 percent (see tables 2 and 3). Consequently, the financial problems faced by many rice producers in Louisiana is relatively unchanged, even with government programs.

The seasonal average market price for rice has been quite variable, ranging from $4.03 per hundredweight in 1986 to $7.65 in 1987, however, market price has increased only 4 percent between 1985 and 1989. Consequently, with declining target prices and increasing costs, returns to rice producers have declined over the period. In the northeast Louisiana rice producing area of the Mississippi River Delta, the situation is about the same as for southwest Louisiana. Consequently, Louisiana rice producers are faced with continued financial difficulty even with the government program as formulated in the 1985 farm bill.

[Tables 1-4 follow:]

TABLE 1

Comparison of estimates of rice costs of production and returns between USDA-ERS and Louisiana State University, Department of Agricultural Economics and Agribusiness, including and excluding direct effects of Government programs, northeast Louisiana, 1988.

	USDA-ERS		
	No Govt. payments	Govt. payments	LSU
Gross value of production:			
Market value	$350.13	$350.13	$335.83
Deficiency payments	0.00	175.13	116.05
Marketing loan proceeds	0.00	19.76	0.00
Haying/grazing on ACR acreage	0.00	0.18	0.00
Total	350.13	545.20	451.88
Less share rent:			
Land rent (⅕ share)	0.00	0.00	45.19
Water rent (⅕ share)	0.00	0.00	45.19
Total share rent	0.00	0.00	90.38
Total value of production, less share rent	350.13	545.20	361.50
Cash expenses:			
Seed	21.25	21.25	14.40
Fertilizer	32.92	32.92	25.65
Chemicals	46.10	46.13	17.20
Custom operation	38.97	38.97	17.71
Fuel, lube, and electricity	43.43	44.27	27.90
Repairs	23.29	23.99	35.45
Hired labor	38.62	39.02	32.75
Purchased irrigation water	0.44	0.44	0.00
Drying	38.51	38.51	41.50
Technical services	0.85	0.85	0.00
Storage	0.00	0.00	25.27
Set-aside maintenance	0.00	0.00	1.99
Miscellaneous	1.31	1.31	1.50
Total variable cash expenses	285.69	287.66	241.32
General farm overhead	20.23	23.22	8.31
Taxes and insurance	11.09	12.98	3.31
Interest on operating loans	11.12	12.77	7.51
Interest on intermediate loans	0.00	0.00	24.50
Interest on real estate	4.69	5.39	13.13
Total fixed cash expenses	47.13	54.36	56.76
Total cash expenses	332.82	342.02	298.08
Value of production less cash expenses	17.31	203.18	63.42
Capital replacement	42.67	44.41	41.18
Value of production less cash expenses and capital replacement	−25.36	158.77	22.24
Economic (full ownership) costs:			
Variable cash expenses	285.69	287.66	241.32
General farm overhead	20.23	23.22	8.31
Taxes and insurance	11.09	12.98	3.31
Capital replacement	42.67	44.41	41.18
Allocated returns to owned inputs:			
Return to operating capital	6.58	6.67	5.46
Return to other nonland capital	10.46	10.88	33.69
Net land rent	49.88	110.80	88.95

	USDA-ERS		
	No Govt. payments	Govt. payments	LSU
Net water rent	0.00	0.00	94.76
Unpaid labor	14.65	14.81	0.00
Total, economic costs	441.25	511.43	516.99
Residual returns to management and risk	−91.12	33.77	−65.11
Harvest-period price ($/cwt.)	6.91	6.91	6.91
Yield (cwt./planted acre)	50.67	50.67	48.60

TABLE 2

Comparison of estimates of rice costs of production and returns between USDA-ERS and Louisiana State University, Department of Agricultural Economics and Agribusiness, including and excluding direct effects of Government programs, southwest Louisiana, 1988.

	USDA-ERS		
	No Govt. payments	Govt. payments	LSU
Gross value of production:			
Market value	$299.09	$299.09	$335.41
Deficiency payments	0.00	165.28	175.25
Marketing loan proceeds	0.00	17.13	0.00
Haying/grazing on ACR acreage	0.00	0.00	0.00
Total	299.09	481.50	510.66
Less share rent:			
Land rent (⅕ share)	0.00	0.00	86.81
Water rent (⅕ share)	0.00	0.00	86.81
Total share rent	0.00	0.00	173.62
Total value of production, less share rent	299.09	481.50	337.04
Cash expenses:			
Seed	28.72	28.72	18.80
Fertilizer	40.74	40.74	25.57
Chemicals	32.50	32.51	21.68
Custom operation	33.09	33.09	25.67
Fuel, lube, and electricity	41.70	41.99	26.37
Repairs	17.26	17.55	39.04
Hired labor	35.05	35.19	35.58
Purchased irrigation water	0.34	0.34	0.00
Drying	41.72	41.72	34.70
Technical services	0.14	0.14	0.00
Storage	0.00	0.00	20.30
Set-aside maintenance	0.00	0.00	1.99
Miscellaneous	0.24	0.32	1.08
Total variable cash expenses	271.50	272.31	250.79
General farm overhead	16.66	18.61	6.68
Taxes and insurance	6.68	7.62	3.46
Interest on operating loans	12.81	14.30	7.38
Interest on intermediate loans	0.00	0.00	22.77

	USDA-ERS		
	No Govt. payments	Govt. payments	LSU
Interest on real estate	4.69	5.23	3.94
Total fixed cash expenses	40.84	45.76	44.23
Total cash expenses	312.34	318.07	295.03
Value of production less cash expenses	–13.25	163.43	42.01
Capital replacement	26.96	27.59	38.27
Value of production less cash expenses and capital replacement	–40.21	135.84	3.75
Economic (full ownership) costs:			
Variable cash expenses	271.50	272.31	250.79
General farm overhead	16.66	18.61	6.68
Taxes and insurance	6.68	7.62	3.46
Capital replacement	26.96	27.59	38.27
Allocated returns to owned inputs:			
Return to operating capital	5.52	5.55	5.37
Return to other nonland capital	6.65	6.81	31.31
Net land rent	47.28	106.88	95.62
Net water rent	0.00	0.00	87.18
Unpaid labor	27.59	27.70	0.00
Total, economic costs	408.84	473.07	518.68
Residual returns to management and risk	–109.75	8.43	–8.02
Harvest-period price ($/cwt.)	6.81	6.81	6.81
Yield (cwt./planted acre)	43.92	43.92	49.25

TABLE 3

Yields, returns, and costs per acre for rice over time, southwest Louisiana, 1985 through 1990.

	1985	1986	1987	1988	1989	1990 (proj.)
Yield	$42.80	$44.48	$44.48	$49.25	$49.25	$49.25
Market price	7.24	4.03	7.65	6.90	7.50	7.50
Gross returns at market price	309.87	179.27	340.29	339.85	369.40	369.40
Gross returns at loan rate plus deficiency payments	473.32	509.60	504.01	515.10	503.58	499.74
Land charge	88.50	95.29	93.95	95.62	94.18	93.57
Water charge	81.37	88.84	87.56	87.18	85.02	84.04
Other cash expenses	289.77	281.97	256.77	295.03	306.62	311.40
Capital replacement	34.98	36.38	35.70	38.27	38.00	38.00
Total specified costs	494.62	502.47	473.98	516.09	523.82	527.00
Residual returns to management and risk:						
Market price	–184.75	–323.21	–133.69	–176.24	–154.42	–157.60
Market price plus Government payments	–21.30	7.13	30.03	–0.98	–20.24	–27.26

Yields, returns, and costs per hundredweight of rice over time, southwest Louisiana, 1985 through 1990.

Southwest Louisiana	1985	1986	1987	1988	1989	1990 (proj.)
Yield	$42.80	$44.48	$44.48	$49.25	$49.25	$49.25
Gross returns at market price	7.24	4.03	7.65	6.90	7.50	7.50
Gross returns at loan rate plus deficiency payments	11.06	11.46	11.33	10.46	10.22	10.15
Land charge	2.07	2.14	2.11	1.94	1.91	1.90
Water charge	1.90	2.00	1.97	1.77	1.73	1.71
Other cash expenses	6.77	6.34	5.77	5.99	6.23	6.32
Capital replacement	0.82	0.82	0.80	0.78	0.77	0.77
Total specified costs	11.56	11.30	10.66	10.48	10.64	10.70
Residual returns to management and risk:						
Market price	−4.32	−7.27	−3.01	−3.58	−3.14	−3.20
Market price plus Government payments	−0.50	0.16	0.68	−0.02	−0.41	−0.55

TABLE 4

Yields, returns, and costs per acre for rice over time, northeast Louisiana, 1985 through 1990.

	1985	1986	1987	1988	1989	1990 (proj.)
Yield	$42.50	$45.00	$48.60	$48.60	$48.60	$48.60
Market price	7.24	4.03	7.65	6.90	7.50	7.50
Gross returns at market price	307.70	181.35	371.79	335.34	364.50	364.50
Gross returns at loan rate plus deficiency payments	470.92	513.32	532.17	491.46	480.55	477.10
Land charge	78.50	85.41	88.95	81.86	79.67	79.51
Water charge	79.55	86.81	94.76	82.47	81.03	79.83
Other cash expenses	278.44	289.10	278.82	298.08	315.29	318.40
Capital replacement	33.58	36.19	36.83	41.18	39.63	39.63
Total specified costs	470.08	497.51	499.36	503.59	515.63	517.37
Residual returns to management and risk:						
Market price	−162.38	−316.16	−127.57	−168.25	−151.13	−152.87
Market price plus Government payments	0.84	15.81	32.81	−12.13	−35.08	−40.27

Yields, returns, and costs per hundredweight of rice over time, northeast Louisiana, 1985 through 1990.

	1985	1986	1987	1988	1989	1990 (proj.)
Yield	$42.50	$45.00	$48.60	$48.60	$48.60	$48.60
Gross returns at market price	7.24	4.03	7.65	6.90	7.50	7.50
Gross returns at loan rate plus deficiency payments	11.08	11.41	10.95	10.11	9.89	9.82
Land charge	1.85	1.90	1.83	1.68	1.64	1.64
Water charge	1.87	1.93	1.95	1.70	1.67	1.64
Other cash expenses	6.55	6.42	5.74	6.13	6.49	6.55
Capital replacement	0.79	0.80	0.76	0.85	0.82	0.82
Total specified costs	11.06	11.06	10.27	10.36	10.61	10.65
Residual returns to management and risk:						
Market price	−3.82	−7.03	−2.62	−3.46	−3.11	−3.15
Market price plus Government payments	0.02	0.35	0.68	−0.25	−0.72	−0.83